Petition

No.

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81-1258

IN THE

Supreme Court of the United States

OCTOBER TERM, 1981

JOHN M. SHAHEEN, SHAHEEN NATURAL RESOURCES COMPANY INC., NEWFOUNDLAND REFINING COMPANY LTD., U.S.A. and FOUNDERS CORPORATION,

Petitioners,

-against-

THE CLARKSON COMPANY LIMITED, as Trustee in Bankruptcy, appointed by the Supreme Court of the Province of Newfoundland, of the property of Newfoundland Refining Company Limited and Provincial Refining Company Limited,

Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

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QUESTIONS PRESENTED

1. Whether the Court of Appeals for the Second Circuit has sanctioned a violation of the due process rights of Petitioners and abrogated principles of comity articulated by this Court in Hilton v. Guyot, 159 U.S. 113 (1945), by affirming a pretrial order of the District Court for the Southern District of New York denying Petitioners' motion to amend their answer (1) to assert that principles of comity preclude the recognition in this country of The Clarkson Company Limited ("CLARKSON") as Trustee in Bankruptcy, appointed by the Supreme Court of the Province of Newfoundland, of the property of Newfoundland Refining Company Limited ("NRC") and Provincial Refining Company Limited ("PRC"); and (2) to assert an affirmative defense alleging a conspiracy claim against CLARKSON and challenging CLARKSON's good faith and standing to institute this suit

as Bankruptcy Trustee in New York by reason of its involvement in a conspiracy to, inter alia, loot and dissipate the assets of NRC and PRC and to throw the NRC/PRC refinery into bankruptcy -- thereby depriving Petitioners of a fair trial and precluding them from attacking both the good faith and motives of CLARKSON in bringing this action and from challenging CLARKSON's standing to institute this action in view of the fact that its appointment as Bankruptcy Trustee in Newfoundland was tainted by a wrongful conspiracy to throw NRC and PRC into bankruptcy and to financially cripple SHAHEEN; and thereby precluding Petitioners from proving to the jury in the trial of this action that CLARKSON instituted this lawsuit as part of and pursuant to a continuing wrongful conspiracy to drive the SHAHEEN refinery out of business by improper means and to financially cripple SHAHEEN.

2. Whether the Court of Appeals for the Second Circuit has sanctioned a violation of the due process rights of the individual Petitioners by affirming their personal liability as directors for corporate transfers totalling some $30 million and by applying a wholly erroneous new and sweeping standard of liability rendering directors virtual insurers contrary to all prior decisions imposing "trust fund" liability, to wit, by finding personal director liability for corporate transfers in the following circumstances:

(a) the transfers began to occur two years prior to the bankruptcy of the transferor company at a time when it was an on-going business entity, although a jury later found that it was experiencing technical or "balance sheet" insolvency at the time of said transfers;

(b) there is no allegation or proof that the directors were aware of any prospects of bankruptcy at the time of the transfers;

(c) there is no allegation or proof that the directors engaged in fraud, deception or misrepresentation in connection with the subject transfers; and

(d) the directors did not personally benefit from or receive the subject transfers for which they are held liable;

whether the Second Circuit turned settled corporate law on its head by holding that directors of a corporation become fiduciaries for the benefit of the unsecured creditors of the corporation whenever the on-going corporation slips into balance sheet insolvency; and whether the Second Circuit was correct (by finding personal director liability to creditors for transfers made by the corporation, regardless of whether the creditors had knowledge of

those transfers, and absent any claim of deception or misrepresentation) in making directors insurers of the success of the enterprise -- a rule of law which, if let stand, would empty corporate boardrooms across America.

THE PARTIES BELOW

The parties below were as follows:

1. The Clarkson Company Limited, Plaintiff,

2. John M. Shaheen, Roy M. Furmark, Albin W. Smith, Peter L. Caras, Paul W. Rishell, Shaheen Natural Resources Company, Inc., Newfoundland Refining Company Ltd. U. S. A. and Founders Corporation, Defendants.

PARENT COMPANIES, SUBSIDIARIES AND AFFILIATES OF FILING CORPORATIONS

1. Shaheen Natural Resources Company, Inc.:

SNR Holdings, Inc. (affiliate)

Newfoundland Refining Company Limited (affiliate)

Provincial Refining Company Limited (affiliate)

2. Newfoundland Refining Company Ltd. U. S. A.:

SNR Holdings, Inc. (parent)

3. Founders Corporation:

Syracuse Television, Inc. (affiliate)

Mill Creek Oil Company Limited (affiliate)

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In The

SUPREME COURT OF THE UNITED STATES

October Term, 1981

No.

In Re

JOHN M. SHAHEEN, SHAHEEN NATURAL RESOURCES COMPANY, INC., NEWFOUNDLAND REFINING COMPANY LTD. U.S.A., and FOUNDERS CORPORATION,

Petitioners,

-against-

THE CLARKSON COMPANY LIMITED, as Trustee in Bankruptcy, appointed by the Supreme Court of the Province of Newfoundland, of the property of Newfoundland Refining Company Limited and Provincial Refining Company Limited,

Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

Petitioners John M. Shaheen ("SHAHEEN"), Shaheen Natural Resources Company, Inc. ("SNR"), Newfoundland Refining Company Ltd.

U.S.A. ("NRC,U.S.A.") and Founders Corporation ("FOUNDERS") respectfully pray that a Writ of Certiorari issue to review the decision of the United States Court of Appeals for the Second Circuit entered on September 15, 1981.*

In said decision, the Second Circuit affirmed, on appeal, the judgment of the United States District Court for the Southern District of New York (Richard Owen, J.), entered July 22, 1981, following a jury trial adjudging Petitioners liable for money damages aggregating some 80 million dollars. Respondent The Clarkson Company Limited ("CLARKSON") obtained this judgment in its capacity as the Trustee in Bankruptcy appointed by the Supreme Court of the Province of Newfoundland of the property of the Newfoundland Refining Company Limited ("NRC") and Provincial

* Petitioners are sometimes referred to as defendants hereinafter.

Refining Company Limited ("PRC"). NRC and PRC (which were owned and controlled by Petitioners prior to their bankruptcy) owned and operated an oil refinery located in Come By Chance, Newfoundland ("REFINERY"). NRC and PRC were adjudicated bankrupt on March 12,1976 and the REFINERY was shut down.

The instant petition addresses itself to a pre-trial order of the District Court, entered February 2, 1978, which denied Defendants' motion to amend their answer to assert an affirmative defense containing a conspiracy claim against CLARKSON and challenging CLARKSON's good faith and standing to institute this suit as Bankruptcy Trustee in New York (pursuant to applicable principles of comity) by reason of its involvement in a conspiracy to, inter alia, loot and dissipate the assets of NRC and PRC and to throw the REFINERY into bankruptcy. By said order, the District Court absolutely

precluded Petitioners from proving to the jury in the trial of this action that CLARKSON instituted this lawsuit as part of and pursuant to a continuing wrongful conspiracy to drive a SHAHEEN refinery out of business by improper means and to financially cripple SHAHEEN.

It is submitted that the District Court deprived Petitioners of a fair trial by so precluding them from attacking both the good faith and motives of CLARKSON in bringing this action and from challenging CLARKSON'S standing to institute this action in view of the fact that its appointment as Bankruptcy Trustee in Newfoundland was tainted by a wrongful conspiracy to throw NRC and PRC into bankruptcy and to financially cripple SHAHEEN.

In addition, the instant Petition addresses itself to the egregious error of the courts below in holding individual defendants personally liable for money

damages aggregating some 50 million dollars.

OPINIONS BELOW

The opinion issued by the Second Circuit is reported at 660 F.2d 506 (2d Cir. 1981). A copy of said decision appears in Appendix D. infra. The relevant memorandum opinion of the district court appears in Appendix B, infra.

JURISDICTION

The decision of the Second Circuit was entered September 15, 1981. A petition for rehearing was denied by order filed November 20, 1981 (Appendix E, infra.) This petition was timely filed. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1) and 28 U.S.C. 1651.

CONSTITUTIONAL PROVISIONS AND STATUTES INVOKED

1. Constitution of the United States, Amendment V: No person ... shall be deprived of life, liberty, or property, without due process of law ... .

STATEMENT OF THE CASE

A. Background

Petitioner JOHN M. SHAHEEN is an independent oil refiner and marketer of crude oil and/or refined petroleum products who competes throughout the world with the major oil companies and consortiums.

SHAHEEN is the sole stockholder of Petitioner SNR, which he owns and controls, and through which he operates.

SHAHEEN, through SNR and other intermediate companies, owned and controlled an 85.6% interest in the underlying assets and profits of NRC, PRC and in the REFINERY at Come By Chance, Newfoundland prior to the bankruptcy of the above entities in March, 1976.

SHAHEEN was and is identified as the controlling force behind NRC, PRC and the REFINERY and said entities were created

by his skills, reputation and credit and are integrally identified with and reflect his skills, reputation and credit.*

Prior to 1973, SHAHEEN and SNR, inter alia, caused the formation of NRC and PRC, and caused the REFINERY to be built. The REFINERY had the most up-to-date equipment and was designed to produce high grade petroleum products, including gasoline and jet fuel.

The REFINERY commenced operation in December, 1973.

In or about September, 1973, NRC entered into an agreement and supplements (hereinafter referred to as the "AGENCY AGREEMENT") with a Japanese company called ATAKA & CO. LTD. ("ATAKA") and its American subsidiary ATAKA AMERICA, INC. ("ATAKA") pursuant to which ATAKA obligated itself

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* Petitioners NRC,U.S.A. and FOUNDERS are companies controlled by SHAHEEN.

to finance the purchase of all of the crude oil for NRC, PRC and the REFINERY.

Under the terms of the AGENCY AGREEMENT, ATAKA was obligated to supply financing of all the crude oil to the REFINERY, and it did so until the bankruptcy of NRC, PRC and the REFINERY in March, 1976.

The AGENCY AGREEMENT contained a "Force Majeure" clause which provided that ATAKA's obligation to finance the purchase of crude oil for the REFINERY would not be excused or abrogated by reason of any default by NRC and/or PRC in their obligations to ATAKA if said default was triggered by "causes deemed Force Majeure".

The AGENCY AGREEMENT contained a "Forum Selection" clause which provided that any disputes arising under it or

between the parties to it in connection with ATAKA's obligation to continue to finance the purchase of crude oil for the REFINERY should be litigated by a New York Court in accordance with New York law.

In or about November, 1975, in view of certain financial problems of the REFINERY which Petitioners alleged below were caused by events of "Force Majeure" within the meaning of the AGENCY AGREEMENT, including, inter alia, the Arab oil embargo, weather and labor conditions, and unanticipated structural and engineering defects and deficiencies in the REFINERY Plant, ATAKA, although continuing to honor its contractual obligations to finance the purchase of crude oil for the REFINERY, demanded that SHAHEEN surrender control of the management of NRC, PRC and the REFINERY to it pending the REFINERY's return to profitability and SHAHEEN did

surrender control to ATAKA.

Subsequently, having gained access to and control of NRC and PRC, and having moved its personnel into the NRC/PRC offices at 90 Park Avenue, New York, New York, ATAKA, pursuant to a wrongful conspiracy, Petitioners alleged below, and acting under the direction of MORGAN STANLEY & CO. ("MORGAN") whom, it was alleged below, sought to financially cripple SHAHEEN and drive him out of the oil business on behalf of its major oil company clients, proceeded to begin to exercise control of the funds and operations of NRC and PRC in order to cause a wrongful bankruptcy, by looting, dissipating, fraudulently diverting and misappropriating the funds of NRC and PRC. Petitioners alleged below that, between November 1975 and February 13, 1976, MORGAN, ATAKA, CLARKSON and other conspirators misappropriated and wrongfully converted to their own use approximately

$20 million to $30 million of the funds of NRC and PRC, thereby appropriating almost all of the funds of NRC and PRC in order to shut NRC and PRC down and to fraudulently drive the REFINERY into bankruptcy.

Further, Petitioners alleged below that, pursuant to the conspiracy to drive the REFINERY into bankruptcy, MORGAN, in conjunction with the SUMITOMO BANK LTD. ("SUMITOMO") and ATAKA, caused the incorporation of ATLANTIC TRADING (DELAWARE) CORPORATION ("ATLANTIC") on December 20, 1975 for the sole purpose of assigning to it ATAKA's purported claims against NRC and PRC to enable ATLANTIC to institute bankruptcy proceedings against NRC and PRC (which ATLANTIC did on February 13, 1976), thereby vitiating the New York Forum Selection and Force Majeure clauses in the financial contract between ATAKA and NRC, thereby vitiating ATAKA's con-

tractual obligation to provide crude oil for the REFINERY and thereby violating Section 489 of the New York Judiciary Law.

On February 13, 1976, having fraudulently depleted the funds of NRC and PRC, as alleged below, and having fraudulently manufactured various defaults by NRC and PRC so as to wrongfully create bankruptcy conditions, as alleged below, ATLANTIC petitioned the bankruptcy court in Newfoundland, on an ex parte application, to appoint Clarkson as interim receiver of NRC and PRC pending a bankruptcy hearing, and Clarkson was so appointed; likewise, on February 13, 1976, ATLANTIC installed Clarkson as a Receiver of PRC's crude oil and refined product inventory at the REFINERY under a FIRST, SECOND and THIRD DEBENTURE purportedly secured by said inventory. Petitioners alleged below that the aforesaid applications for the

appointment of the Interim Receiver by the Newfoundland court and the actions taken by ATLANTIC in installing CLARKSON as Receiver of PRC's inventory were all taken in violation and breach of the AGENCY AGREEMENT.

It was further alleged below that MORGAN, ATAKA and CLARKSON fraudulently concealed the above-stated fraudulent misappropriations of NRC and PRC funds which caused the financial problems of NRC and PRC from the Newfoundland Bankruptcy Court.

In March, 1976, ATLANTIC argued to the Bankruptcy Court in Newfoundland that NRC and PRC were "indebted" to it at least in the sum of $1,000 in order to satisfy the conditions of the Canadian bankruptcy statute which requires that a bankruptcy petition must be dismissed unless the petitioning creditor can prove a debt owing to it in the sum of $1,000. ATLANTIC argued that certain promissory notes and/or bills of exchange issued by NRC and/or

PRC (pursuant to the AGENCY AGREEMENT pursuant to which ATAKA was obligated to finance the purchase of crude oil for the REFINERY) to ATAKA constituted debts to it.

NRC and PRC argued that said instruments were covered by the applicable "Force Majeure" clause in the AGENCY AGREEMENT and that, under said "Force Majeure" clause, the subject instruments were not debts "due and owing" to ATAKA. In addition, NRC and PRC argued that the interpretation of said instruments was governed by the applicable "forum selection" clause in the AGENCY AGREEMENT and that, therefore, the question whether a debt was "due and owing" must be decided by a New York Court in accordance with New York Law.

ATLANTIC, by means of false and fraudulent representations and arguments, as alleged below, caused the Newfoundland Bankruptcy Court to find that there was no "bona fide" dispute regarding whether the subject instruments

were "due and owing" because the subject instruments upon which ATLANTIC based its petition did not come under the ambit of the subject "force majeure" and "forum selection" clauses; whereas, in fact, the subject instruments were governed by said clauses. Based on the above findings, NRC and PRC were adjudicated bankrupt by the Newfoundland Court and CLARKSON was appointed bankruptcy trustee. It is submitted that subject findings of the Canadian Bankruptcy Court are in derogation of the laws and public policy of the State of New York and of the United States and should not be recognized under applicable principles of law, equity and comity. The Canadian Courts ignored and in fact destroyed the AGENCY AGREEMENT; the Canadian Courts refused to abide by or honor the forum selection and force majeure clauses in the AGENCY AGREEMENT; and the Canadian Courts' findings that the promissory notes

and bills of exchange upon which ATLANTIC predicated its bankruptcy petition were not governed by the terms of the AGENCY AGREEMENT is absolutely repugnant to the laws and public policy of the United States. The Canadian Bankruptcy Court refused to entertain and did not consider relevant any of the conspiracy claims of Petitioners.

B. The Instant Lawsuit

CLARKSON instituted this lawsuit in its capacity as the Trustee in Bankruptcy, appointed by the Supreme Court of the Province of Newfoundland, of the property of NRC and PRC.

CLARKSON instituted this lawsuit for the purported purpose of marshalling the assets of NRC and PRC on behalf of its creditors, including ATAKA. However, Petitioners alleged below that CLARKSON instituted this lawsuit pursuant to an ongoing and continuing conspiracy to finan-

cially destroy SHAHEEN, not to benefit the bankrupt estate.

Indeed, Petitioners alleged below that, subsequent to the bankruptcy adjudications:

(a) CLARKSON breached its fiduciary duties by failing to marshal the assets of NRC and PRC, by protecting the other conspirators, by failing to enforce claims of NRC, PRC and the bankrupt estate against the conspirators, by affirmatively participating in and concealing the subject conspiracy, and by failing to press ATAKA to fulfill its obligations under the AGENCY AGREEMENT to continue to supply crude oil to the REFINERY;

(b) CLARKSON failed to attempt to recoup the above-noted misappropriations and has fully cooperated and participated in the above-stated misappropriations and other wrongful acts in furtherance of the conspiracy despite its position as bank-

ruptcy trustee; and, despite its knowledge of said wrongs, has done nothing to stop them or challenge them; and

(c) the conspirators (including CLARKSON) having succeeded in shutting down and mothballing the REFINERY, prevented SHAHEEN from regaining the REFINERY.

C. The Nature of the Instant Lawsuit and the Error Committed Below

There are two bases for this appeal: (1) pre-trial error; and (2) error committed at trial.

1. The Pre-Trial Error

CLARKSON originally commenced this action in the Federal District Court for the Southern District of New York (Richard Owen, J.) on March 26, 1976, by order to show cause, seeking an order requiring defendants to turn over the books and records of NRC and PRC. At that point in time, no claims for money damages had

yet been asserted. It was merely a turnover proceeding.*

Defendants opposed CLARKSON's request for NRC's books and records by challenging its standing to maintain any action in New York by reason of its involvement in a fraudulent conspiracy to loot NRC and PRC, to throw NRC and PRC into bankruptcy, to release ATAKA from ever-increasing liabilities to NRC and PRC, and to drive SHAHEEN out of business in Newfoundland.

The district court dismissed defendants' claims and granted relief to CLARKSON. On appeal, the Court of Appeals for the Second Circuit affirmed (544 F.2d 624), holding:

> "...Clear and convincing evidence of fraud is required in order successfully to attack a foreign judgment, just as such proof is necessary before a court will set aside its own judgment [cita-

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* The basis for federal jurisdiction was diversity of citizenship.

> tions omitted]. While appellants are free to introduce additional proof at a trial on the merits of this action, they have not shown enough at this stage to cast doubt on the Canadian judgment." (Id., at 631)

Subsequently, on February 23, 1977, defendants sought discovery against CLARKSON regarding its participation in the alleged conspiracy. However, such discovery was effectively denied. Thus, the district court, on March 23, 1977, on CLARKSON's application, granted an ex parte stay of all discovery pending CLARKSON's motion for summary judgment. Said stay was in effect until February 1, 1978 when the lower court, inter alia, denied defendants' motion to amend their answer to assert their conspiracy claims against CLARKSON. Thus, defendants were never permitted to engage in discovery regarding their conspiracy claims.

The denial by the district court of

defendants' motion to amend their answer to assert their conspiracy claims is one basis for the instant appeal.

2. The Trial Error

Subsequent to the commencement of this action in 1976, CLARKSON was permitted to amend its complaint to assert damage claims against defendants. CLARKSON asserted four basic claims at trial:

(a) that NRC, in the period 1972-1975, had made "due on demand" loans to defendants in the approximate sum of $50 million and that defendants had breached their contractual obligations to repay said loans to CLARKSON (as bankruptcy trustee) on demand;

(b) that defendants had violated Sections 273, 274 and 276 of the New York Debtor and Creditor Law by causing a promissory note and related agreements to be executed in October 1975 between NRC and defendants which provided that said $50 million in advances from NRC to defendants should be repayable June 30, 1985;

(c) that defendants violated the above-enumerated sections of the Debtor and Creditor Law by causing NRC, in the years 1974 and thereafter, to

make advances approximating $30 million to defendants without consideration at a time when NRC was insolvent; and

(d) that the individual defendants (officers and/or directors of NRC) breached their fiduciary obligations to NRC and creditors thereof in causing the foregoing events.

Defendants, by contrast, asserted as follows at trial:

(a) that the subject $50 million in advances constituted long-term investments by ATAKA in various Shaheen enterprises; that ATAKA intended NRC to be nothing more than a middleman in connection with said advances; and that said advances were repayable by the Shaheen organization and SNR to ATAKA on June 30, 1985 and were not due on demand;

(b) that the October 1975 promissory note and related documentation merely embodies the original intention that the subject advances were due in 1985 and, therefore, was not fraudulent;

(c) that the subject $30 million in advances from NRC to defendants were not fraudulent conveyances under the Debtor and Creditor Law in any event because: (1) NRC was solvent in 1974 and thereafter at the time it made said advances; and (2) there was consideration for said advances in view of the original intention of ATAKA and in view of the

fact that NRC was merely a middleman or intermediary; and

(d) that the individual defendants have not breached any fiduciary obligations to anyone.

Following a jury trial held in June, 1980, a jury found: (1) that NRC and/or PRC had made "due on demand" claims to defendants; (2) that said loans violated the New York Debtor and Creditor Law; and (3) that the individual defendants John M. Shaheen, Roy M. Furmark, Albin W. Smith, Peter L. Caras, and Paul W. Rishell (who were all officers and/or directors of NRC) had breached their fiduciary duties to NRC and its creditors by permitting the above-noted transfers to occur and were, therefore, individually liable for damages caused by the transfers.* Total damages (equalling the amount of the subject transfers) were

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* A copy of the "Special Questions" answered by the jury is appended hereto in Appendix A.

assessed at approximately $50 million, which sum was apportioned among the individual defendants on a percentage basis. SHAHEEN was held individually liable for approximately 70% of the transfers, or approximately $30 million.

The second basis for this appeal is that the courts below erred in making the corporate directors of NRC (the individual defendants herein) trustees of NRC's assets for the benefit of creditors the moment NRC slipped into balance sheet insolvency.

D. The Relevant Decisions and Appeals Below

By memorandum decision and order dated February 1, 1978, the district court denied defendants' motion to amend their answer to assert their conspiracy claims against CLARKSON. A copy of said decision is appended hereto in Appendix B. A copy of defendants' motion to

amend their answer to assert their conspiracy affirmative defense and proposed affirmative defense is appended hereto in Appendix C.*

The decision of the Court of Appeals for the Second Circuit affirming the district court's denial of defendants' motion to assert their conspiracy claims against CLARKSON by way of affirmative defense and affirming the jury trial verdict as against the individual defendants based upon breach of their fiduciary duties is reported in Clarkson v. Shaheen, 660 F.2d 506 (2d Cir. 1-81). A copy of said decision appears in Appendix D hereto.

By decision filed November 20, 1981, the Second Circuit denied defendants' motion for rehearing. A copy of said decision is appended hereto in Appendix E.

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* Also appended hereto in Appendix C is additional evidentiary material (including Petitioners' answer and counterclaim below which was also dismissed by the District Court) establishing the conspiracy to drive the REFINERY into bankruptcy which was before the District Court when it dismissed Petitioners' conspiracy claims.

REASONS FOR GRANTING THE WRIT

As noted above, the instant petition is based upon two grounds:

(a) that the courts below erred in dismissing Petitioners' conspiracy pleading for legal insufficiency (without granting leave to re-plead) prior to the trial of this action on the ground that the conspiracy pleading failed to satisfy the particularity requirements of Rule 9(b) of the Federal Rules of Civil Procedure; and

(b) that the courts below erred in applying a wholly erroneous new and sweeping standard of liability rendering directors virtual insurers contrary to all prior decisions imposing "trust fund" liability.

Petitioners respectfully submit that this petition should be granted because the Second Circuit has sanctioned

judicial proceedings in the District Court which so far depart from the accepted and usual course of judicial proceedings as to call for an exercise of this Court's power of supervision.

Extraordinary relief is sought for six reasons:

(a) it is respectfully submitted that the courts below, in applying the Rule 9(b) particularity requirements to a conspiracy pleading, adopted a rule of law which has the effect of absolutely precluding any plaintiff from ever pleading an actionable conspiracy in view of the fact that conspiracies are by their very nature secretive and cannot be pleaded with particularity but must be pleaded "upon information and belief" pursuant to the less stringent requirements of Rule 8 of the Federal Rules of Civil Procedure;

(b) this case involves a question of exceptional importance regarding Petition-

ers' basic due process rights to a fair trial and a full hearing, especially given the staggering sums involved and the devastating effect of the judgment on the personal reputation and credit of Petitioners for the balance of their lives.

(c) this case involves a question of exceptional importance regarding the applicability of Rules 8 and 9 (Federal Rules of Civil Procedure) to conspiracy pleadings;

(d) consideration by this Court is necessary to secure the uniformity of decisions with respect to the applicability of Rules 8 and 9 to a conspiracy pleading and in view of a prior decision of the Second Circuit which expressly held, prior to the trial of this action, that Petitioners herein were entitled to attack at trial the standing, good faith and motives of CLARKSON and to establish that CLARKSON's appointment as

Bankruptcy Trustee was tainted by virtue of the fact that said appointment originated in a bankruptcy artificially caused by a wrongful conspiracy and, therefore, was tainted with fraud:

> "...Clear and convincing evidence of fraud is required in order successfully to attack a foreign judgment, just as such proof is necessary before a court will set aside its own judgment (citations omitted). While appellants are free to introduce additional proof at a trial on the merits of this action, they have not shown enough at this stage to cast doubt on the Canadian judgment." (Emphasis supplied) (Clarkson v. Shaheen, 544 F.2d 624, 631 (2d Cir.1976);

(e) the courts below egregiously violated the due process rights of Petitioners and abrogated the principles of comity articulated by this Court in Hilton v. Guyot, 159 U. S. 113 (1945) by refusing to permit Petitioners to plead and prove that principles of comity preclude the recognition of CLARKSON as a bankruptcy trustee in this country because its ap-

pointment in Newfoundland was tainted with fraud; and

(f) the courts below turned settled corporate law on its head by holding that directors of a corporation become fiduciaries for the benefit of the unsecured creditors of the corporation whenever an on-going corporation slips into balance sheet insolvency. Indeed, by finding personal director liability to creditors for transfers made by the corporation, regardless of whether the creditors had knowledge of those transfers, and absent any claim of deception or misrepresentation, the Second Circuit would make directors insurers of the success of the enterprise -- a rule of law which, if let stand, would empty corporate boardrooms across America.

ARGUMENT

I.

PETITIONERS' CONSPIRACY PLEADING PRESENTS A VALID TRIABLE ISSUE WHICH SHOULD HAVE GONE TO THE JURY

The Second Circuit appears to have affirmed the District Court's dismissal of Petitioners' conspiracy pleading on three grounds:

(a) in that the pleading failed to satisfy the pleading requirements of F.R.C.P. 9(b);

(b) in that the same claims were previously litigated and rejected in the Newfoundland bankruptcy proceedings; and

(c) in that prior lawsuits asserting supposedly similar claims have been dismissed.

None of these grounds affords a proper basis for dismissal of the subject pleading.

It is submitted that the Second Cir-

cuit failed to give Petitioners a fair hearing with respect to the legal sufficiency of their conspiracy pleading. The Second Circuit did not even address or refer to the underlying facts that were pleaded as evidence of the conspiracy. Rather, the Second Circuit, without addressing the merits of the pleading, dismissed it summarily, stating:

> "The remaining claims of error merit only brief mention. The district court's denial of the Shaheen defendants' motion to amend their answer to assert unparticularized allegations of fraud in the Newfoundland bankruptcy proceeding and Clarkson's appointment was proper."

A. THE PLEADING FULLY SATISFIES THE RELEVANT PLEADING REQUIREMENTS

1. The Pleading Itself

A conspiracy pleading must allege two essential elements:

(a) a conspiracy to accomplish a wrongful purpose; and

(b) overt acts taken by the conspir-

ators in furtherance of the conspiracy which constitute actionable wrongs, to wit, the underlying facts establishing the conspiracy.

These elements are well-pleaded in the subject affirmative defense* which alleges a conspiracy to accomplish the following wrongful purposes:

(a) to drive the SHAHEEN REFINERY into an artificial and wrongfully induced bankruptcy by, inter alia, looting and dissipating the assets of NRC and PRC;

(b) to vitiate, breach, caused to be breached, interfere with, evade, and avoid ATAKA's contractual obligation to finance

* A copy of the proposed affirmative defense conspiracy pleading and motion to amend is appended hereto in Appendix C. Also appended hereto in Appendix C is Petitioners' answer and counterclaim below which was also dismissed by the District Court. Said counterclaim was before the District Court at the time it dismissed the subject affirmative defense pleading and contained additional evidentiary material establishing the conspiracy to drive the REFINERY into bankruptcy.

the purchase of crude oil for the REFINERY, thereby wrongfully enabling ATAKA and SUMITOMO to escape from their mounting financial obligations to the REFINERY;

(c) to vitiate the forum selection and force majeure clauses in the financial contracts pursuant to which ATAKA was obligated to finance the purchase of crude oil for the REFINERY;

(d) to drive SHAHEEN as an independent refiner out of business in Newfoundland;

(e) to replace an independent refiner (SHAHEEN) with a more cooperative ally or minion or close to the REFINERY;

(f) to drive SHAHEEN out of the oil business, period.*

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* The subject affirmative defense conspiracy pleading must be read in the light of the full record before the District Court at the time the District Court dismissed the pleading. That record fully discloses evidentiary detail regarding the conspiracy.

The pleading also alleges and the record before the District Court fully discloses numerous overt wrongful acts done in furtherance of the conspiracy which constitute circumstantial proof of the conspiracy, to wit:

(a) through the intercessions of SUMITOMO, ATAKA retained MORGAN to assist it in devising a scheme to wrongfully avoid, breach and/or vitiate its financial obligation to provide crude oil for the REFINERY until at least 1985; and CLARKSON participated in the plotting, in consideration of its eventual appointment as bankruptcy trustee.

(b) subsequently, SHAHEEN was notified that the conspirators would "pull the plug" on the REFINERY -- although they possessed no legal or business justification for doing so -- unless he would relinquish control of the REFINERY on a temporary basis pending its return to

profitability;

(c) likewise, at about the same time, ATAKA threatened to cut off the financing of crude oil for the REFINERY -- which it had no legal right to to because it was contractually obligated to continue to provide said financing at least through 1985 -- unless SHAHEEN would relinquish control of the REFINERY on a temporary basis as noted above;

(d) subsequently, acting under duress and coercion, and acting in the best interests, as he perceived them, of the creditors of the REFINERY and of the employees of the REFINERY in the face of wrongful threats to "pull the plug" and shut down the REFINERY, SHAHEEN, unaware of the conspiracy to shut down the REFINERY in any event, agreed, inter alia, to grant ATAKA personnel entry and access to his 90 Park Avenue, New York offices, to inspect the books and records of NRC

and PRC, and to participate in the control and management of NRC and PRC;

(e) subsequently, having gained access to and control of NRC and PRC, and having moved its personnel into the NRC/PRC offices at 90 Park Avenue, New York, New York, ATAKA, pursuant to the conspiracy, acting under the direction of MORGAN and SUMITOMO, proceeded to begin to exercise control of the funds and operations of NRC and PRC in order to cause a wrongful bankruptcy, by looting, dissipating, fraudulently diverting and misappropriating the funds of NRC and PRC;

(f) between November 1975 and February 12, 1976, SUMITOMO and/or ATAKA misappropriated and wrongfully converted to their own use approximately $20 million to $30 million of the funds of NRC and PRC, thereby appropriating almost all of the funds of NRC and PRC in order to shut NRC and PRC down;

(g) on or about December 16, 1975, ATAKA, in breach of its financial obligation to finance the purchase of crude oil for the REFINERY, caused the flow of crude oil to the REFINERY to cease by refusing to permit the unloading of a cargo of crude oil carried by the GOLAR BETTY which had arrived at the REFINERY;

(h) ATAKA, in breach of its existing financial obligation to finance the purchase of crude oil for the REFINERY, demanded, on December 16, 1975, that, as a condition precedent to unloading of the GOLAR BETTY, PRC issue a $25 million debenture ("SECOND DEBENTURE") payable February 15, 1976, in payment for the GOLAR BETTY oil, the only alternative was the shutting down of the REFINERY;

(i) the SECOND DEBENTURE provided that all sums available to pay the FIRST DEBENTURE and secured as collateral under the FIRST DEBENTURE should be diverted to pay

the SECOND DEBENTURE, thereby creating a behicle whereby (1) ATAKA could loot and bleed the funds of NRC and PRC by means of the SECOND DEBENTURE (and avoid voidable preference bankruptcy problems); (2) cause a default under the FIRST DEBENTURE; and (3) use the event of the FIRST DEBENTURE default to accelerate the due date of the SECOND DEBENTURE;

(j) MORGAN, in conjunction with SUMITOMO and ATAKA, caused the incorporation of ATLANTIC on December 20, 1975 for the sole purpose of assigning to it ATAKA's purported claims against NRC and PRC to enable ATLANTIC to institute bankruptcy proceedings against NRC and PRC (which ATLANTIC did on February 13, 1976), thereby vitiating the New York Forum Selection and Force Majeure clauses in the financial contract between ATAKA and NRC, thereby vitiating ATAKA's contractual obligation to provide crude oil for the REFINERY and

and thereby violating Section 489 of the New York Judiciary Law; and

(k) subsequent to the bankruptcy adjudication, CLARKSON breached its fiduciary duties by failing to marshal the assets of NRC and PRC, by protecting the other conspirators, by failing to enforce claims of NRC, PRC and the bankrupt estate against the conspirators, by affirmatively participating in and concealing the subject conspiracy, and by failing to press ATAKA to fulfill its obligations under the AGENCY AGREEMENT to continue to supply crude oil to the REFINERY;

The subject pleading flatly states that CLARKSON was part of the conspiracy (para. 25) and the circumstantial evidence is fully set forth: CLARKSON, with knowledge of the wrongful acts, did nothing to stop them or challenge them (para. 42).

Finally, the pleading contains allegations, stated upon information and be-

lief, that CLARKSON aided ATLANTIC in wrongfully instituting bankruptcy proceedings (para. 23).

2. The General Standards To Be Employed On A Motion To Dismiss A Pleading For Legal Insufficiency

Dismissal of a pleading for legal insufficiency is a drastic remedy. Nagler v. Admiral, 248 F.2d 319, 322 (2d Cir.1957). Accordingly, the following standards must be employed:

(a) all allegations must be accepted as true. Build of Buffalo v. Sedita, 441 F.2d 284, 287 (2d Cir. 1971);

(b) the pleading must be liberally construed to achieve substantial justice. Rule 8(f);

(c) a pleading should not be dismissed for legal insufficiency unless it appears to a certainty that plaintiff is entitled to no relief under any state of facts which could be proved in support of the claim. Build of Buffalo v. Sedita,

supra; 2A Moore's Federal Practice, section 12.08; and

(d) it is black-letter law that a pleading should not be dismissed for legal insufficiency prior to the completion of discovery where the opposing party possesses material information not in the possession of the pleader. In such a case, leave to re-plead at the end of the discovery process should be permitted.

3. The Validity of the Subject Conspiracy Pleading Must be Judged by the Standards of Rule 8

Volume 2A, Moore's, sec. 8.17(5),which deals with conspiracy pleadings, states as follows:

> "As they do to pleadings in other civil actions, the general principles of "notice pleadings" under Rule 8 apply to pleadings averring conspiracy. However, while Rule 8 demands only a "short and plain statement of the claim showing that the pleader is entitled to relief," in a pleading of conspiracy it is important that within the pleader's ability to do so, and without going into unnecessary detail, the opposing party be informed of the nature of the conspiracy

> charged, to which he may adequately plead. (Footnotes omitted)

Even the Second Circuit has, in the past, clearly recognized that Rule 8 applies to conspiracy pleadings. Nagler v. Admiral, 248 F.2d 319 (2d Cir. 1957). Accord: Gretener v. Dyson, 298 F.Supp. 350 (S.D.N.Y. 1969)*

4. The Gross Error of the District Court

The District Court committed gross error in dismissing Petitioners' conspiracy pleading:

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* Rule 8 requires only that the pleader set forth his claim in such a manner as to enable his opponent to prepare a responsive pleading. Conspiracy and combination can only be proven from circumstantial evidence. Makan v. Trenton, 3 P.R.D. 429 (D.N.J. 1944). Conspiracy by its very nature is secretive and, pursuant to Rule 8, courts will liberally construe allegations concerning combination and conspiracy. The "combination" element of conspiracy is pleaded with sufficient specificity if the complaint merely alleges that the defendants conspired. Vazquez v. Ferre, 404 F. Supp. 815 (D.N.J. 1975); Heart Disease v. General Motors, 463 F.2d 98, 100 (2d Cir. 1972); Powell v. Board, 327 F.2d 131 (2d Cir. 1964).

(a) it erred in applying Rule 9(b) to a conspiracy pleading. In fact, such a pleading must allege the conspiracy "upon information and belief" since conspiracies are secretive. They are only known from their effects and must be inferred from circumstantial evidence. "Information and belief" allegations are certainly permissible under Rule 8, when supported by circumstantial evidence or overt acts in furtherance of the alleged conspiracy;*

(b) it erred in focusing exclusively upon the allegations relating to CLARKSON's participation in the conspiracy. Even assuming arguendo that CLARKSON was unaware of the conspiracy, applicable principles of comity nonetheless require that the conspiracy defense be permitted to be

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* Many such overt acts are alleged in the subject pleading upon knowledge (not upon information and belief).

pleaded and proven because, if a conspiracy existed, CLARKSON'S appointment as bankruptcy trustee was "tainted with fraud" and, therefore, said appointment should not be recognized in the United States;

(c) it erred in finding that all allegations linking CLARKSON to the conspiracy were "on information and belief".* Petitioners alleged as fact (not upon information and belief) that CLARKSON participated in the conspiracy, inter alia, by knowingly permitting the other conspirators to dissipate the assets of NRC and PRC (paras. 24, 25, 26, 27, 28, 40 and 42) and by affirmatively assisting them in accomplishing actionable wrongs (paras. 25, 27). Although active participation of CLARKSON is adequately alleged, a conspirator need

* In fact, the only such allegations alleged "on information and belief" are stated in portions of paragraphs 23 and 24. These isolated allegations relate only to certain activities of CLARKSON and not to the remainder of the conspiracy which is not alleged "upon information and belief".

not actively participate in wrongdoing so long as he has knowledge thereof and ratifies it. Darraugh v. Carrington, 264 App. Div. 126, 34 N.Y.S.2d 742 (1st Dept. 1942), Nederlandsche v. Schreiber, 17 App.Div.2d 783, 232 N.Y.S.2d 644 (1st Dept. 1962); Harte v. Shayaui, 33 Misc.2d 680, 227 N.Y.S.2d 538 (Dist.Ct. N.Y.Co. 1962):

> When it is determined that the defendant entered into the bargain or design and it is also found that he enjoyed its fruits, it is not necessary for the court to find that he actively participated further in the accomplishment of the design. Although passive and silent, he is equally culpable as the active malefactor (Place v. Minster, et al., supra, p. 96)

Indeed, even if CLARKSON were an unknowing participant, its appointment would still be tainted and it would lack standing to sue by reason of the conspiracy of the other named parties to artificially create the bankruptcy;*

* The Second Circuit and the District Court ignored the fact that all of the allegations relating to the conspiracy of the other named parties were not upon information and belief and stood on their own.

(d) it erred in finding that overt acts or failures to act by CLARKSON after the formation of the conspiracy do not constitute circumstantial evidence linking CLARKSON to the conspiracy at the time of its appointment as Bankruptcy Trustee. The law is settled that because participation in a conspiracy at its formation must be inferred from circumstantial evidence, action following its formation must necessarily be used as circumstantial evidence to prove participation in its formation. Thus, in Keviczky v. Lorber, 250 N.Y. 297, 302 (1943), the New York Court of Appeals stated:

> Direct and positive proof of a conspiracy to cheat and defraud such as is here presented is seldom, if ever, attained. Conspiracies of this nature ordinarily are not conceived and executed openly but in secret. Usually the only evidence available is that of disconnected acts on the part of the individual conspirators, which acts, however, when taken together in connection with each other, show the conspiracy to secure a particular result quite as satisfactori-

> ly and conclusively as more direct proof. (People v. Flack, 125 N.Y. 324; People v. Van Tassel, 157 N.Y. 561.

Accord: U.S. v. Johns-Manville, 1 F.R.D. 548, 550 (E.D. Ill. 1941)

B. THE SECOND CIRCUIT HAS PREVIOUSLY RULED THAT PETITIONERS ARE ENTITLED TO PLEAD AND PROVE THEIR CONSPIRACY CLAIM AT TRIAL

The Second Circuit previously held that the foreign bankruptcy judgment could be and should be collaterally attacked in the trial of this action.

The Second Circuit addressed the relevant issue in Clarkson v. Shaheen, 544 F.2d 624 (2nd Cir. 1976), wherein SHAHEEN appealed from an order granting CLARKSON a preliminary injunction entitling it to possession of the books and records of NRC and PRC:

> Even assuming that the allegations of fraud made in the state court action were sufficiently brought to the attention of Judge Owen, allegations of fraud in the state suit are not sufficient of themselves to show that the bank-

> ruptcy declaration and appointment of Clarkson as trustee were 'tainted with fraud.' (at 630) (emphasis added)
>
> * * *
>
> A foreign judgment may not be collaterally attacked 'upon the mere assertion of the party that the judgment was erroneous in law or in fact,' Hilton v. Guyot, supra, 159 U.S. at 203, 16 S.Ct. at 158, much less upon a mere assertion of fraud. Clear and convincing evidence of fraud is required in order successfully to attack a foreign judgment, just as such proof is necessary before a court will set aside its own judgment, Nederlandsche Handel-Maatschappij, N.V. v. Jay Emm, Inc., 301 F.2d 114, 115 (2d Cir. 1962); 11 C. Wright & A. Miller, supra, § 2860, at 189. While appellants are free to introduce additional proof at a trial on the merits of this action, they have not shown enough at this stage to cast doubt on the Canadian judgment." (at 631) (emphasis added)

Despite the foregoing, the lower courts have adamantly refused to permit Petitioners to conduct discovery on their defense or to introduce proof of their defense at trial.

The law is well settled that the adjudication in bankruptcy of a company is not res judicata as respects a claim that the bankruptcy proceedings themselves were ini-

tiated in fraud or as respects the financial condition of the company at the time of the bankruptcy. Thus, in Page v. Clark, 119 Misc. 110, 195 N.Y.S. 529 (Sup.Ct. Cayuga Co. 1922), Aff. 208 App.Div. 827 (4th Dept. 1924), rev. on other grounds, 239 N.Y. 403 (1925), the New York Supreme Court stated:

> The adjudication in bankruptcy of the company is not res judicata as to the financial condition of the company at the time that the alleged fraud was perpetrated. The claim is that the bankruptcy proceedings were initiated in fraud. There is no attack made on the regularity of the proceedings themselves. The defendants now urge that the bankruptcy proceedings protect them against any claim of damage by the plaintiff. In other words, they seek to take advantage of their own fraud. This the law will not permit them to do. Where the institution of the proceedings is the basis of the claim of fraud, the adjudication is not res judicata as to the financial condition of the company, because the propriety of the proceedings is involved as an issue of fraud.

Likewise, the Court of Appeals stated:

> Undoubtedly the theory of the learned trial justice was correct

> that the fraud, if established, set in motion a train of disaster and that defendants cannot negative the fraud by proving the disaster.

Likewise, in Hilton v. Guyot, 159 U.S. 113 (1945), this Court recognized that a prior judgment may always be collaterally attacked on the ground that it was procured by fraud:

> When an action is brought in a court of this country, by a citizen of this country, by a citizen of a foreign country against one of our own citizens, to recover a sum of money adjudged by a court of that country to be due from the defendant to the plaintiff, and the foreign judgment appears to have been rendered by a competent court having jurisdiction of the cause and of the parties, and upon due allegations and proofs and opportunity to defend against them, and its proceedings are according to the course of a civilized jurisprudence, and are stated in a clear and formal record, the judgment is prima facie evidence, at least, of the truth of the matter adjudged; and it should be held conclusive upon the merits tried in the foreign court, unless some special ground is shown for impeaching the judgment, as by showing that it was affected by fraud or prejudice, or that by the principles of international law and by the comity of our own country it should not be given full credit and effect. (at 205-206)

Clearly, Petitioners should have been permitted to prove at trial that principles of comity preclude the recognition of CLARKSON as a bankruptcy trustee in the United States because its appointment was tainted with fraud.

The law of this country is clear that when a foreign judgment is procured by fraud or violates the public policy of the United States, it will not be recognized or given effect in the United States. Likewise, the appointment of a trustee in bankruptcy by a foreign court does not in itself give such trustee standing to bring suit in this country. Such standing may only be recognized pursuant to principles of comity. Oakey v. Bennett, 52 U.S. 33 (1851); In re Waite, 99 N.Y. 433 (1885); Vladikavkazsky Ry. Co. v. N.Y. Trust Co., 263 N.Y. 360 (1934); and Bank of Buffalo v. Vesterfelt, 232 N.Y.S.2d 783 (Co. Ct. Erie Cty. 1962).

C. THE PRIOR DISMISSALS OF RELATED SUITS WERE NOT ON THE MERITS

Although a number of lawsuits relating to Petitioners' conspiracy claims have been dismissed on procedural or technical grounds, the question of the merits of the subject lawsuits has never been addressed. Therefore, the subject dismissed suits cannot constitute an estoppel of or bar to Petitioners' conspiracy claims.

Each of the previously dismissed suits was a stockholder derivative suit and each of said suits was dismissed on a procedural ground endemic to stockholder derivative suits and irrelevant anywhere else. Not one of the subject derivative suits was dismissed on the merits.

D. CONCLUSION WITH RESPECT TO PETITIONERS' AFFIRMATIVE DEFENSE

It is submitted that the courts below have run roughshod over the basic due process right of Petitioners in absolutely

barring them from establishing that, pursuant to a wrongful conspiracy, CLARKSON instituted the instant lawsuit on fraudulent grounds solely to further cripple SHAHEEN -- not to marshall the assets of NRC and PRC on behalf of their creditors.

The very crux of Petitioners' defense at trial should have been that CLARKSON instituted this suit as part of a larger conspiracy to cripple SHAHEEN and destroy the REFINERY. Indeed, Petitioners had an absolute due process right to demonstrate to the jury CLARKSON's conspiratorial motive in characterizing the intercompany advances as fraudulent and to show that the bankruptcy judgment was void.

The denial of the rights of discovery and defense to these Petitioners violates basic procedural rules and decisions of this Court dictating liberality and even-handedness in evaluating the legal sufficiency of pleadings and in grating amend-

ments of pleadings.

The jury was confronted with the spectacle of a "sacrosanct" Bankruptcy Trustee dutifully marshalling assets. Petitioners were not permitted to establish that the Bankruptcy Trustee was a fraud. The trial was a simple miscarriage of justice.

II.

THE COURTS BELOW ERRED IN IMPOSING PERSONAL LIABILITY UPON THE INDIVIDUAL DEFENDANTS

Individual defendants were sued in their capacity as directors of NRC and one such director (SHAHEEN) was held personally liable for the amount of approximately $30 million by reason of the fact that, for a period of two years preceding the bankruptcy, NRC loaned some $30 million to affiliated companies -- not to SHAHEEN personally or individually.

Explicitly declining to "examine the claim (by SHAHEEN and others) that the

trustee may not sue on NRC's or the shareholder's behalf" by reason of estoppel and ratification by the shareholder, the Second Circuit held that the Trustee "may sue on behalf of the creditors". Ignoring the fact that there was no claim of fraud, deceit or misrepresentation, the Second Circuit found individual defendants liable to the Trustee for a "breach of the fiduciary duty owed to creditors" of NRC simply because they "knew or should have known of (the) advances".

While CLARKSON itself admitted that "(n)owhere does the trustee allege that [individual defendants] engaged in fraudulent misrepresentation" (CLARKSON'S Supplemental Trial Brief at 2), the jury was compelled by the District Court's charge to return a verdict resulting in a ruinous judgment of approximately $50 million against individual defendants for "breach of the fiduciary duty owed to creditors..."

It is only under this sweeping revision of established law, positing the existence over a two-year period of a fiduciary duty of directors of an on-going, operating corporation to the creditors of that corporation, that the judgment against individual defendants could be affirmed.

In reaching this anomalous result, the Second Circuit misapprehended basic points of law and fact which were before it, and issued an opinion contrary to the settled law of this land and of the State of New York on an issue of "exceptional importance" -- i.e., the duties owed by a director of a corporation to the shareholders and the creditors, respectively.

The crucial errors in the Second Circuit's decision -- which, if left uncorrected, will establish untenable precedent-- can be summarized as follows:

(a) Turning settled corporate law on its ear, the Second Circuit held that direc-

tors of a corporation become fiduciaries for the benefit of the unsecured creditors of the corporation whenever an on-going corporation slips into balance sheet insolvency. Indeed, by finding personal director liability to creditors for transfers made by the corporation, regardless of whether the creditors had knowledge of those transfers, and absent any claim of deception or misrepresentation, the Second Circuit would make directors insurers of the success of the enterprise -- a rule of law which, if let stand, will empty corporate boardrooms across America;

(b) Ignoring settled-law to the contrary, the Second Circuit held that a corporate director who received no transferred funds can be held personally liable in damages for transactions which are reversible under the New York Fraudulent Conveyances Act (N. Y. Debtor and Creditor Law §§ 270 et seq. (McKinney 1980 Supp.) if he

"knew or should have known" of the existence of such transfers;

(c) The Second Circuit let stand a compound finding of the jury that individual defendants breached fiduciary duties it held were simultaneously owing both to the corporation and its creditors without even considering whether CLARKSON was estopped from asserting the claim of breach of duty to the corporation, without reconciling the obvious conflict of such duties, and offering no authority for the novel proposition that a Trustee in Bankruptcy may assert claims on behalf of unsecured creditors.

Under the rule of the Second Circuit, a finding of fraud or misrepresentation on the part of directors is not a prerequisite for liability. All that is necessary is that a director "knew or should have known" of a transaction which was later determined to have violated the technical provisions

of the Fraudulent Conveyances Act. Under such circumstances the director can be liable in damages to a Trustee in Bankruptcy empowered to sue in the name of the unsecured creditors for the amounts of the transfers despite the fact that the Fraudulent Conveyances Act provides that the sole remedy under that Act is reversal of the transaction.

Under such a rule a director's first instinct will be to dissolve the corporation at the first hint of financial difficulty, thus placing him in a position at odds with the interests of the shareholders to whom he holds the highest duty. Failure to shut down immediately would be to invite personal financial ruin if the company ultimately failed. In short, the Second Circuit rule holds a director liable, as a fiduciary, to creditors as soon as a company slips into balance sheet insolvency. He then becomes, in effect, an insurer for

the benefit of unsecured creditors of the success of any steps which might be taken to revive a financially troubled corporation.

Judge Cardozo explained the proper scope of the trust fund duty as follows: "The duty of directors to creditors upon liquidation of the assets is that of trustee to beneficiary." John H. Giles Dyeing Machine Co. v. Klauder-Weldon Dyeing Machine Co., 233 N.Y. 470, 476, 135 N.E. 854, 856 (1922). (Emphasis added.) Another commentator has noted:

> "Ordinarily a corporation must be both insolvent and have ceased to do business before a trust attaches to its funds and properties for the benefit of creditors." 15A Fletcher Cyclopedia of Corporations § 7386 (Perm. Ed.) (Emphasis added).

The Second Circuit, however, overlooked the facts in the trust fund cases, misapprehended their significance and created a new rule of law. It upheld the District Court's charge which required the jury to

evaluate expert testimony as to the value of corporate assets years before bankruptcy, determine whether the corporation was technically insolvent at that time (despite balance sheets showing it as solvent) and to hold individual defendants to the standard of the creditors' fiduciary -- a trustee of the corporate assets for the benefit of unsecured creditors.

The Second Circuit, perhaps in an attempt to justify this conclusion, implies that the transactions in question were something more sinister than loans, referring to the money as being "'loaned'" to SHAHEEN and his companies. In so doing, the Second Circuit has misapprehended the record. The individual defendants were not alleged to have engaged in fraud or misrepresentation of any kind. To the contrary, the creditors on whose behalf CLARKSON purports to sue were aware of the transactions in question. CLARKSON pro-

ceeded under the theory that "(t)his lawsuit isn't about anybody deceiving the unsecured creditors... The unsecured creditors may have known, didn't know or did know, I don't care." (A. 873-74.) Moreover, the District Court conducted the trial and excluded evidence under the assumption that the creditors had full knowledge of the transactions. (A. 1514). Accordingly, in holding individual defendants liable to unsecured creditors, who knew of and acquiesced in the transactions and who were not misled in any way, the Second Circuit has held individual defendants to the standard of an insurer for the creditors.

Prior to the instant decision the law in the Second Circuit (and other circuits) and in New York was well settled that the New York Fraudulent Conveyances Act (N.Y. Debtor and Creditor Law §§ 270, et seq., (McKinney 1980 Supp.) does not permit recovery of damages against a non-transferee

of a fraudulent conveyance. It provides only for recovery, from the transferee, of the property fraudulently conveyed.* In holding that the trust fund doctrine attaches upon balance sheet insolvency, the Second Circuit has turned this rule on its ear. It held that non-recipients of fraudulent transfers can be held liable in damages under the New York Fraudulent Conveyances Act.

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* Chichester v. Golden, 321 F.2d 250, 253 (9th Cir. 1963); Duell v. Brewer, 90 F.2d 59, 60 (2d Cir. 1937); Cunningham v. Merchants' National Bank, 4 F.2d 25, 31 (1st Cir. 1925). See also 4 Collier on Bankruptcy, ¶ 67.451 at 608 (14th Ed. 1978); Elliott v. Gluchon, 390 F.2d 514, 517 (9th Cir. 1967); Eyges v. Boylston National Bank, 294 F. 286 (D. Mass. 1923); Vinlis Construction Co. v. Roreck, 67 Misc.2d 942, 947, 325 N.Y.C.2d 457, 463 (Sup.Ct. Nassau Co. 1971), aff'd, 43 A.D.2d 911, 351 N.Y.S.2d 648 (2d Dept. 1974); Levy v. Paramount Public Corp., 149 Misc. 129, 266 N.Y.S. 271 (Sup.Ct. N.Y.Co. 1933), aff'd, 241 A.D. 711, 269 N.Y.S. 977 (1st Dept.), aff'd, 265 N.Y. 629, 193 N.E. 418 (1934); Island Paper Co. v. Carthage Timber Corp., 128 Misc. 246, 218 N.Y.S. 346 (Sup.Ct. Jefferson Co. 1926).

CONCLUSION

For the reasons stated above, a Writ of Certiorari should issue to review the judgment and opinion of the United States Court of Appeals for the Second Circuit.

Respectfully submitted,

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APPENDIX

APPENDIX A

SPECIAL QUESTIONS SUBMITTED TO AND ANSWERED BY THE JURY

Clarkson v. Shaheen 76 Civ. 1373

Special Questions for the Jury

(1) Were the loans or advances to

1) John M. Shaheen

2) Shaheen Natural Resources Company, Inc.

3) Newfoundland Refining Company Ltd., USA

4) Founders Corporation

made from 1972 through 1975, carried on the NRC books and records, in fact due on demand?

Yes X No

If the answer is "Yes," you should go on to question (2). If the answer to this question is "no," go to question (3) directly.

(2) What were the net amounts of said loans or advances made by NRC on the date of demand for payment by the

trustees as of NRC on the date of demand for payment by the trustee as of March 13, 1976 to the following:

1) John M. Shaheen $501,231

2) Shaheen Natural Resources Company, Inc. $46,049,040

3) Newfoundland Refining Company Ltd., USA $2,344,268

4) Founders Corporation $548,392

3) Did the loans or advances by NRC described above made during 1974 and 1975 violate section 273 of the Debtor and Creditor Law?

Yes X No ____

4) Did the said loans or advances made during 1974 and 1975 violate section 274 of the Debtor and Creditor Law?

Yes X No ____

5) Did the Promissory Note and Letter Agreement, executed in October 1975, violate section 276 of the Debtor

and Creditor Law?

Yes X No

6) Did said Promissory Note and Letter Agreement violate section 273 of the Debtor and Creditor Law?

Yes X No

7) Did the said Promissory Note and Letter Agreement violate section 274 of the Debtor and Creditor Law?

Yes X No

8) Was there a breach of fiduciary duty to NRC and its creditors with respect to (a) the making of loans and advances in 1974 or 1975 by the following individual defendants:

John M. Shaheen	Yes X	No
Roy M. Furmark	Yes X	No
Albin W. Smith	Yes X	No
Peter L. Caras	Yes X	No
Paul W. Rishell	Yes X	No

(b) the making of the Promissory Note of October 1975 by the following individual defendants:

John M.haheen	Yes X	No ____
Roy M. Furmark	Yes X	No ____
Albin W. Smith	Yes X	No ____
Peter L. Caras	Yes X	No ____
Paul W. Rishell	Yes X	No ____

9) Do you find that NRC was insolvent at the time of

(a) the loans or advances

Yes X No ____

(b) the Promissory Note

Yes X No ____

10) If your answer to any of the defendants listed in 8 (a) above is "Yes," what damage do you find plaintiff was caused by each such defendant:

John M. Shaheen	74% of $30,609,026
Roy M. Furmark	20% of $30,609,026

Albin W. Smith	2% of $30,609,026
Peter L. Caras	2% of $30,609,026
Paul W. Rishell	2% of $30,609,026

APPENDIX B

DECISION OF DISTRICT COURT DENYING PETITIONERS LEAVE TO AMEND THEIR ANSWER TO PLEAD AN AFFIRMATIVE DEFENSE THAT THE APPOINTMENT OF CLARKSON AS BANKRUPTCY TRUSTEE WAS TAINTED WITH FRAUD

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

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THE CLARKSON COMPANY LIMITED, as Trustee in Bankruptcy, appointed by the Supreme Court of the Province of Newfoundland, of the property of Newfoundland Refining Company Limited and Provincial Refining Company Limited,

Plaintiff,

-against-

JOHN M. SHAHEEN, ROY M. FURMARK, ALBIN W. SMITH, PHILIP GANDERT, PETER L. CARAS, PAUL W. RISHELL, WILLIAM J. SHERIDAN and JOHN DOE,

Defendants.

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Index No. 76 Civ. 1373

MEMORANDUM AND ORDER

Filed U. S. District Court February 2, 1978

OWEN, District Judge

Before me for determination are the following motions:

(1) A motion by the plaintiff trustee in bankruptcy for leave to file an amended summons and complaint adding additional parties defendant and asserting claims for money damages totaling more than $52,000,000 against the various defendant corporations and the defendant officers and directors of them and the bankrupts NRC and PRC:

(2) Motions by the original defendants for (a) leave to file an amended answer to plead fraud by plaintiff as an affirmative defense to plaintiff's cause of action for permanent possession of the books and records of the bankrupts PRC and NRC: (b) discovery as to the allegations of fraud in the proposed amended answer in advance of my determination of plaintiff's motion for summary judgment;

and (c) a cross-motion by plaintiff for a protective order striking certain interrogatories and document requests and staying all discovery pending the outcome of plaintiff's motion for summary judgment;

(3) A motion by plaintiff for summary judgment granting it permanent possession of the books and records of NRC and PRC, which it already has pursuant to a preliminary injunction; and

(4) Motions by plaintiff for (a) orders of attachment against various of the defendants named in its proposed amended complaint in the total sum of more than $5,000,000 and (b) expedited discovery in aid of attachment.

1. The plaintiff's motion to amend.

The plaintiff trustee is new in possession of the books and records of the bankrupts, which possession was originally the sole relief sought by this action. Plaintiff, based on an examination thereof,

now moves to amend the complaint to allege certain monies due for various reasons.

The general rule is that leave to amend should be freely granted, F.R.Civ. P. 15(a). The grounds for denying such leave are bad faith on the part of the moving party or resulting prejudice to another party. Absent one of these factors, mere delay in moving to amend, which is interposed by defendants in opposing the motion, is an insufficient basis for denying the motion. Middle Atlantic Utilities Co. v. S.M.W. Development Corp., 392 F. 2d 380 (2d Cir. 1968); United States v. International Business Machines Corp., 66 F.R.D. 223 (S.D.N.Y. 1975).

Here, none of the original defendants has shown that granting the motion to amend the complaint in the form proposed by plaintiff would result in

legal prejudice to him,[1] or that plaintiff is acting in bad faith. Accordingly, plaintiff's motion for leave to amend as modified by the Sussman affidavit of September 14, 1977 is granted.

2. The original defendants' motion to amend their answer and the related motions for discovery and for a protective order.

The original defendants have moved to amend their answer to interpose a Sixth Affirmative Defense to the plaintiff's claim for a permanent injunction which would give plaintiff permanent possession of the books and records of NRC and PRC. Defendants would allege the plaintiff trustee's bad faith and fraudulent behavior in connection with NRC's and PRC's

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1. A typical example of legal prejudice occurs when a defendant seeks to amend his answer to plead the statute of limitations long after suit has been instituted, thereby precluding plaintiff from initiat-

bankruptcy declarations and plaintiff's appointment as trustee in the Canadian bankruptcy proceedings.

They rely on the Court of Appeals opinion in Clarkson Co. v. Shaheen, 544 F. 2d 624 (2d Cir. 1976) (hereinafter cited as "Clarkson"), affirming my order granting plaintiff a preliminary injunction giving it possession of the books and records at issue. The relevant language in the opinion is as follows:

> Even assuming that the allegations of fraud made in the state court action were sufficiently brought to the attention of Judge Owen, allegations of fraud in the state suit are not sufficient of themselves to show that the bankruptcy declaration and appointment of Clarkson

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1. (continued
ing litigation in another jurisdiction in a timely fashion. E.g., Strauss v. Douglas Aircraft Co., 404 F.2d 1152 (2d Cir. 1968). Here, defendants Smith and Sheridan claim that the amendment should not be allowed against them unless jurisdiction over them is independently established for the new claims for relief alleged, because they have moved out of

> as trustee were "tainted with fraud." No independent substantiation of these charges, which must be pleaded "with particularity" under Fed.R.Civ.P. 9(b), was offered.
>
> ...A foreign judgment may not be collaterally attacked "upon the mere assertion of the party that the judgment was erroneous in law or in fact," . . . much less upon a mere assertion of fraud. Clear and convincing evidence of fraud is required in order successfully to attack a foreign judgment, just as such proof is necessary before a court will set aside its own judgment . . . . While appellants are free to introduce additional proof at a trial on the merits of this action, they have not shown enough at this stage to cast doubt on the Canadian judgment.

Id. at 630-31 (footnotes and citations omitted).

The proposed amended answer, however, insofar as it alleges that the declarations

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1. (continued)
New York State. They have submitted no authority for this position and I have found none. I conclude that once a court has obtained personal jurisdiction over a party, the court's power to adjudicate a closely related claim cannot depend on a party's remaining in the jurisdiction. The claim could have been pleaded originally, and defendants Smith and Sheridan's objection to the amendment does not rise to the

of bankruptcy of NRC and PRC and the appointments of Clarkson as trustee were "tainted with fraud," does not meet the pleading requirements of F.R.Civ.P. 9(b).

One problem with the proposed pleading is apparent from ¶¶ 22-27 of the said Sixth Affirmative Defense. To the extent that it pleads wrongdoing by plaintiff at all,

> [t]he allegations violate the general rule that Rule 9(b) pleadings cannot be based on "information and belief." While the rule is relaxed as to matters peculiarly within the adverse parties' knowledge, the allegations must then be accompanied by a statement of the facts upon which the belief is founded.

Segal v. Gordon, 467 F.2d 602,608 (2d

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1. (continued
level of legal prejudice. At best, it is an argument that they would prefer to defend where they now live.

Some of the original defendants also object to the amendment on the ground that it vastly expands the scope of the action from a limited one for permanent possession of books and records to one including claim for damages in excess of $52,000,000, and they point out that I granted plaintiff's motion to dismiss defendants Shaheen and

Cir. 1972) (footnotes omitted); 2A J. Moore, Federal Practice ¶ 9.03 at 1928-29 (2d ed. 1975). For example, ¶ 23 states that "[o]n information and belief, . . . Clarkson gave advice on how the intricate receivership and bankruptcy laws could be invoked on the basis of ex parte fraudulent affidavits, which were the basis for Clarkson's appointment . . . ." Nowhere is it stated what the basis for the information or belief is. Paragraphs 24-26 allege on information and belief that plaintiff was offered its trusteeships upon express agreements with several corporations that it protect certain of them by not seeking retribution in its capacity as trustee. Again, nowhere is the basis for the information and belief stated.

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1. (continued)
Furmark's counterclaims seeking over $600,000,000 in damages from this plaintiff as well as other proposed counterclaim defendants. However, the grounds for the said dismissal were that the counterclaims were permissive and unsupported by the necessary independent jurisdictional basis.

The failure of these defendants to plead with the required specificity is not surprising in light of the admissions by counsel in the memorandum accompanying the motion to amend the answer. It shows the violation of yet another basic principle that allegations of fraud should be made "only after a wrong is reasonably believed to have occurred to seek redress for a wrong, not to find one." Segal v. Gordon, supra, 467 F.2d at 607-08. I refer particularly to the Manning, Carey & Redmond Memorandum of Law on behalf of Shaheen and the corporate defendants filed April 7, 1977:

> The "limited issue" here involved is whether Clarkson's appointment as Trustee was so tainted by fraud as to cause this Court to deny recognition in New York to Clarkson as Trustee.
>
> . . .
>
> Certainly relevant are the circumstances of
>
> (a) how Clarkson came to be recommended for this lucrative job;

(b) any commitments Clarkson may have made to Atlantic Trading (Delaware) Corp. ("Atlantic"), Ataka & Co., Ltd. ("Ataka Japan"), Ataka America, Inc. ("Ataka America"), The Sumitomo Bank, Ltd. ("Sumitomo") -- or to Morgan Stanley & Co., Inc. ("Morgan") acting for them;

(c) any knowledge which Clarkson may have had of the intent of the overall plan -- whether it was innocent, as alleged, or was part of a wrongful plan to cause the breach of the Agency Agreement by Atlantic and escape the consequences thereof;

(d) the extent to which Clarkson may have been aware of the illegality of the assignment of the claims from Ataka to Atlantic;

(e) any "deals" made between the various creditors which Clarkson agreed to effectuate.

The problem is that all of this information, if it exists, is in Clarkson's possession. If Clarkson did nothing illegal, then discovery will prove that.

Id. at 5-6 (emphasis supplied).

I note that many of the allegations against Clarkson assert that it has not performed properly since receiving its appointment as bankruptcy trustee. See ¶ 42 of the Sixth Affirmative Defense in the

Proposed Amended Answer. That, of course, is not a pleading that an appointment "was tainted with fraud." Furthermore, the allegations of violation of the forum-selection clause and of the New York Judiciary Law § 489, see Clarkson, supra, 544 F.2d at 631-32, have been rejected time and again. Thus, they too do not allege a basis for conspiracy charges against plaintiff.

Since the Sixth Affirmative Defense in the Proposed Amended Answer does not satisfy the pleading requirements of F.R. Civ.P.9(b), the motion to amend is denied. Accordingly, defendants' motion for discovery into its allegations of fraud in advance of a determination of plaintiff's motion for an order of summary judgment giving it permanent possession of the books and records of NRC and PRC is denied, and plaintiff's motion for a protective order is granted.

[remainder of opinion is omitted]

APPENDIX C

PETITIONERS' MOTION BELOW TO AMEND THEIR ANSWER TO ASSERT AN AFFIRMATIVE DEFENSE; PETITIONERS' PROPOSED AFFIRMATIVE DEFENSE; AND PETITIONERS' ANANSWER AND COUNTERCLAIM BELOW

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

THE CLARKSON COMPANY LIMITED, as Trustee in Bankruptcy, etc.,

Plaintiff,

-against-

JOHN M. SHAHEEN, et al,

Defendants.

Index No. 76 Civ. 1373 (R.O.)

ORDER TO SHOW CAUSE

Upon reading and filing the annexed affidavit of Richard deY. Manning, Esq. sworn to on March 28, 1977, and the exhibit annexed thereto, it is

ORDERED that the plaintiff or its attorneys show cause before Hon. Richard

Owen, at Room 1505, United States Court House, Foley Square, New York, New York, on the 7th day of April 1977, at 12:00 o'clock in the afternoon of that day, or as soon thereafter as counsel can be heard, why an Order should not be granted, pursuant to FRCP 15(a), granting leave to the defendants to file an amended answer herein on the ground that justice so requires, and it is further

ORDERED that service by hand of a copy of this Order To Show Cause and the papers upon which it is based upon White & Case, attorneys for the plaintiff, on or before 12:00 o'clock noon on the 31st day of March, 1977, shall be deemed sufficient.

Dated: New York, New York
March 28, 1977

(s) Richard Owen
U. S. D. J.

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

THE CLARKSON COMPANY LIMITED, as Trustee in Bankruptcy, etc.,

Plaintiff,

-against-

JOHN M. SHAHEEN, et al,

Defendants.

Index No. 76 Civ. 1373 (R.O.)

AFFIDAVIT

STATE OF NEW YORK)
: SS.:
COUNTY OF NEW YORK)

RICHARD deY. MANNING, being duly sworn, deposes and says:

I am a member of the firm of Manning, Carey & Redmond, attorneys for defendants, and I am familiar with all pleadings and prior proceedings herein. I make this affidavit in support of the motion of the defendants for an order, pursuant to Rule 15 of the FRCP, granting leave to the defendants to file an amended answer herein.

An order to show cause is sought because, on March 24, 1977, the plaintiff sought, and this Court granted, an order to show cause on the plaintiff's motion for summary judgment and a protective order. Deponent believes that it is appropriate that the instant motion be heard at the same time as the plaintiff's motion. As the plaintiff's motion is scheduled to be heard on March 31, 1977, deponent has insufficient time to bring this motion on by ordinary notice.

This affidavit and the accompanying memorandum of law deal with the relief sought on the instant motion. A further affidavit and memorandum in opposition to the plaintiff's motion will be served on or before March 30, 1977, as directed by this Court.

This action was brought by The Clarkson Company Limited ("Clarkson") as trustee in bankruptcy, appointed by the

Supreme Court of Newfoundland, Canada, of Provincial Refining Company Limited ("PRC") and Newfoundland Refining Company Limited ("NRC"). The relief sought is an order of permanent injunction requiring the defendants, who are officers and directors of PRC and NRC, to deliver to Clarkson possession of all property of NRC and PRC, including the books and records of those corporations. An order of preliminary injunction was granted by this Court after a hearing on April 1, 1976.

The answer filed by the defendants herein denied the material allegations of the complaint and set up five affirmative defenses. In addition, defendants John M. Shaheen and Roy M. Furmark asserted eight separate counterclaims against the plaintiff and other counterclaim defendants. By notice of motion dated July 9, 1976, the counterclaim defendants moved to dismiss the counterclaims. The motion was granted

and the counterclaims dismissed by order of this Court dated March 11, 1977.

It is clear from an examination of the counterclaims that the defendants' principal challenge to the right of Clarkson to take possession of the bankrupt's property lies in their allegation that Clarkson participated in a fraudulent conspiracy to bring about the bankruptcy adjudication.

It is respectfully submitted that the defendants have the right to interpose affirmative defenses based upon the trustee's bad faith. In fact, the Second Circuit has so held. In its decision on the defendants' appeal from the aforementioned order of preliminary injunction, the Court said:

> "Clear and convincing evidence of fraud is required in order successfully to attack a foreign judgment, just as such proof is necessary before a court will set aside its own judgment...<u>While appellants are free to introduce additional proof</u>

> at a trial on the merits of this action, they have not shown enough at this stage to cast doubt on the Canadian judgment." (emphasis supplied) Clarkson Company Ltd. v. Shaheen, 544 F.2d 624, 631 (2nd Cir. 1976)

The Second Circuit decided the appeal on November 1, 1976, at which time the counterclaims were pending before this Court. In light of their subsequent dismissal, it would appear that amendment of the answer, in the form annexed hereto as Exhibit "A", would be proper. The purpose of this amendment is to include, as affirmative defenses to the plaintiff's complaint, the matters which were formerly pleaded as counterclaims against the plaintiff and other counterclaim defendants.

The Court's observation that the defendants are free to introduce such proof was an apparent recognition of this rule that the grant or denial of a preliminary injunction does not constitute an adjudication on the merits, nor is it the law of

the case, Federal Waste Paper Corp. v. Garment Cent. Capitol, 268 A.D. 230, 51 N.Y.S.2d 26 (1st Dept. 1944).

In a related State Court action, the Appellate Division, First Department, has recognized that the issue of the trustee's fraud cannot be resolved at this early stage:

> "Thus, at this stage of the action, there is no taint or fraud shown with regard to Clarkson's appointment or status so as to preclude our recognition of Clarkson as the validly appointed trustee in bankruptcy of PRC and NRC." (emphasis supplied) SNR Holdings, Inc. v. Ataka America, Inc., 388 N.Y.S.2d 909, 912

This Court has ruled that the plaintiff is entitled to a preliminary injunction and that ruling has been affirmed on appeal. That is the only holding by which the defendants are bound. It does not mean that the plaintiff is entitled to a permanent injunction and it certainly cannot be construed as a bar to the assertion of valid defenses to the complaint.

No previous application has been made for this relief.

WHEREFORE, deponent respectfully requests an order granting leave to serve and file an amended answer in the form annexed hereto.

(signed)
Richard deY. Manning

Sworn to before me this
28th day of March 1977

(signed)
Muriel Colligan
Notary Public, State of N.Y.
No. 215761555

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

THE CLARKSON COMPANY LIMITED, as Trustee in Bankruptcy, appointed by the Supreme Court of the Province of Newfoundland, of the property of Newfoundland Refining Company Limited and Provincial Refining Company Limited,

Plaintiff,

-against-

JOHN M. SHAHEEN, ROY M. FURMARK, ALBIN W. SMITH, PHILIP GANDERT, PETER L. CARAS, PAUL V. PISHELL, WILLIAM J. SHERIDAN and JOHN DOE,

Defendants.

Index No. 76 Civ. 1373 (R.O.)

AMENDED ANSWER

[Prior portions of answers are omitted]

Sixth Affirmative Defense

(1) Ataka & Co., Ltd. ("Ataka Japan") is a Japanese corporation doing business in New York.

(2) Ataka America, Inc. ("Ataka America") is a New York corporation with its

principal place of business in New York (Ataka Japan and Ataka America are referred to herein collectively as "Ataka").

(3) Atlantic Trading (Delaware) Corp. ("Atlantic Trading") is a Delaware corporation, organized December 19, 1975. It is licensed to do business in New York and its principal place of business is in New York.

(4) The Sumitomo Bank ("Sumitomo") is a banking corporation, incorporated under the laws of Japan, with an agency in New York. Sumitomo is Ataka's principal banker.

(5) Morgan Stanley & Co., Inc. ("Morgan") is a Delaware corporation. Its principal place of business is in New York.

(6) Kleinwort Benson Limited ("Kleinwort") is a United Kingdom corporation. It has an office and is engaged in business in New York.

(7) Government of the Province of Newfoundland and Labrador, Canada ("Province") is a provincial government, which acted in purely a commercial, non-governmental, capacity in all matters herein described, and did business in New York in connection with the matters alleged herein.

(8) The Sanko Steamship Company ("Sanko") is a Japanese company. It is charterer of three crude oil ships to NRC. On information and belief, one of Sanko's principal bankers is Sumitomo.

(9) Plaintiff Clarkson & Co. Limited ("Clarkson"), is a corporation organized under the laws of a Province of Canada. It is doing business in New York. This affirmative defense is directed to Clarkson in its private corporate capacity, and its capacity as purported Trustee of NRC and PRC pursuant to an Order of the Newfoundland Supreme Court dated March 12, 1976,

on the sole application of Atlantic Trading.

(10) PRC owns an oil refinery at Come By Chance, Newfoundland, Canada, which refinery, by contractual agreement was to be supplied crude oil by defendant NRC at its cost.

(11) By an "Agency Agreement", dated September 20, 1973, between NRC as principal and as agent of PRC, Ataka Japan, and Ataka America, Ataka became the "exclusive purchase and sales agent for ALL THE CRUDE OIL contracted by NRC with its suppliers to sell to [PRC]..."; and Ataka undertook and agreed to purchase and pay for all crude oil contracted for by NRC.

(12) In the Agency Agreement Ataka agreed to extend to NRC credit facilities for any advance to be made to NRC's crude oil supplier.Ataka agreed to provide financing "to enable NRC to overcome start-up difficulties in the initial start-up

stage until the refining operation has reached the normal scheduled production stage."

(13) The repayment scheme under the Agency Agreement was such that the only source Ataka could look to for recompense, if PRC did not pay for the crude oil was a $3 million letter of credit, and if that letter was drawn upon, and not replensihed, Ataka could call a default and all outstanding obligations of NRC and PRC would become due, unless such failure to replenish was due to reasons of force majeure.

(14) By practical construction of the Agency Agreement over a period of two years, the parties clearly evidenced their recognition that Ataka had no choice under the circumstances but to continue to finance the crude oil purchases, even in the face of the mounting losses; it was bound so to do under its interpretation

of the contract during this two year period. Moreover, Ataka's managing director guaranteed PRC that Ataka would never exercise its right to call upon the letter of credit as it did not do until after commencement of the conspiracy described below when the unpaid bills of exchange exceeded $275,000,000.

(15) The management of NRC and PRC gave accurate written financial reports to Ataka of the losses being incurred at the refinery but, on information and belief, Ataka gave misleading reports to its lead banker, Sumitomo, telling Sumitomo that all was going well at the refinery.

(16) On information and belief, sometime in 1975, Sumitomo began to realize all was not going well and managed to glean sufficient information to bring the seriousness of the situation to the attention of its management.

(17) In an endeavor to improve its

very exposed unsecured credit position, as lender of the funds to Ataka, which Ataka used to pay for the crude oil Sumitomo, unsuccessfully sought a Third Mortgage on the refinery.

(18) When that failed and the Japanese press received word of the tremendous losses being suffered by Ataka, Sumitomo acting directly, or through Ataka, in November or December, 1975, retained Morgan Stanley & Co., Inc. ("Morgan") to advise it as to how

(a) Ataka could disengage itself from its recognized liability under the Agency Agreement, as construed by Ataka for two years; and

(b) Ataka could collect the claims of Ataka against NRC and PRC and thus pay Ataka's bank loans.

(19) Morgan, in conjunction with Sumitomo and the Ataka companies caused the incorporation of Atlantic Trading (Delaware)

Corp., on or about December 20, 1975, for the specific purpose of assigning to it the Agency Agreement and the Ataka claims against NRC and PRC, which was done by two assignment agreements executed in and under the laws of New York on December 31, 1975 and January 30, 1976. Two weeks thereafter, the bankruptcy proceedings in Newfoundland were instituted solely on the assigned claims. This was an express violation of §489 of the Judiciary Law of New York.

(20) Clarkson was appointed Interim Receiver by the Newfoundland Court on the sole application of Atlantic on the basis of the assigned claims, Receiver and Manager under the Three Debentures assigned by Ataka to Atlantic, and Receiver and Manager under the First Mortgage on the refinery held by Kleinwort and, under the Second Mortgage held by the Province, and later appointed Trustee by the Court on the sole

application of Atlantic.

(21) The purpose of all of this was to avoid the New York forum selection clause in the Agency Agreement, breach the obligation to supply financing for the crude oil and seek to collect the claims of Ataka against NRC and PRC in violation of the Agency Agreement.

(22) Clarkson's wrongdoing in connection with the foregoing was such as to disqualify it as a fiduciary in Canada and further to require the refusal to recognize it by any United States Court.

(23) On information and belief, Clarkson was an active participant in the fraudulent scheme entitled "Project Winnit"; Clarkson gave advice on how the intricate receivership and bankruptcy laws could be invoked on the basis of ex parte fraudulent affidavits, which were the basis of Clarkson's appointment, and which, apparently under the laws of Newfoundland,

cannot be inquired into when the matter is reviewed on the merits; Clarkson covered for and protected from judicial scrutiny -- in violation of its fiduciary duty -- the knowing breach of the New York forum selection clause in the Agency Agreement and, the knowing breach of §489 of the Judiciary Law of New York, on which Clarkson's appointment as Trustee was necessarily based.

(24) The reason Clarkson has so acted in all of these respects is simple -- Morgan, Ataka, Sumitomo and Atlantic, acting through Atlantic, on information and belief, recommended Clarkson as Trustee on the express understanding and agreement that Clarkson would protect Ataka and Sumitomo's interests, subject only to the rights of the First and Second Mortgages, who agreed to the scheme because they, as secured creditors, had nothing to lose.

(25) Clarkson is and was a party to an illegal and fraudulent pact not to seek retribution against Ataka, not to press NRC and PRC claims for breach of contract and fraud, not to harm Ataka or Sumitomo in any way and, after more than a year, has done nothing to force any of them to account for their actions. That was the basis of Clarkson obtaining this very lucrative arrangement -- the Trusteeship of the largest bankruptcy in Canada.

(26) Specifically, Clarkson was offered the very lucrative position of Interim Receiver of NRC and PRC, Trustee of NRC and PRC, Manager and Receiver of assets of NRC and PRC under the First, Second and Third Debentures issued by PRC to Ataka (and assigned to Atlantic), and as Receiver and Manager of the assets secured by the First and Second Mortgages on the Come By Chance refinery held by

Kleinwort and the Province, respectively, for the specific consideration set forth above.

(27) Under the circumstances Clarkson is not entitled to recognition by any New York Court by way of comity or otherwise. This illegal scheme to violate the contract rights of NRC and PRC and to violate the criminal laws of New York could not and would not have been effectuated without the full and complete cooperation of Clarkson.

(28) The relationship between Morgan, Sumitomo, the Ataka companies, Atlantic, Sanko and Clarkson, and the obvious fact that a conspiracy existed among them, and Kleinwort and the Province as well, is demonstrated by the events hereinafter described.

(29) In early November, at Ataka and Sumitomo's request, PRC opened a bank account in Sumitomo's New York Agency;

the only signatories were officers or employees of Ataka, i.e., PRC had no control of the funds.

(30) The principal customers of PRC's refined products were instructed to make payment into the Sumitomo account.

(31) During November and December, 1975, Ataka wrongfully took $18,000,000 of PRC's money and converted it to Ataka's own use.

(32) During December, Sumitomo caused Ataka to cause $3,500,000 of PRC's money to be paid to Sanko, in Sumitomo's words, "to solve an urgent Sanko matter" which, on information and belief, was to make a payment due Sumitomo from Sanko. PRC was not indebted to Sanko for one penny then or ever. Sanko was the charter of certain ships to NRC, but had no connection with PRC.

(33) On December 24, 1975, Ataka drew down a $3,000,000 letter of credit of PRC's

which it had guaranteed it would never do.

(34) On February 13, 1976, pursuant to Morgan's plan for collection of Sumitomo's loans to Ataka, and on the instructions of Sumitomo, Atlantic caused the issuance of an ex parte Interim Receivership Order against NRC and PRC, and such order provided that the Interim Receiver

> "...bring any such property of [NRC and PRC] and their bank accounts located outside Canada within such interim receiver's possession and control...."

This is a specific and unequivocal order that Clarkson, as Interim Receiver, shall bring under its control, inter alia, the PRC account in the New York Agency of Sumitomo.

(35) Sumitomo not only knew of the issuance of this Order but on information and belief instructed Atlantic to cause the Order to be issued and caused Clarkson to be appointed Interim Receiver to carry out that order.

(36) However, on the same date the order was entered, and with full knowledge thereof, Sumitomo breached the Order by removing $2,637,926.85 from PRC's bank account, thus removing it from the possession of Clarkson, the Interim Receiver which Sumitomo had caused to be appointed to take charge of the same account.

(37) On the following Tuesday, February 17, 1976, as part of the carefully orchestrated plan, "Project Winnet" authored by Morgan to collect as much of Sumitomo's money as it could, on information and belief Sumitomo caused Sanko (for whom Sumitomo had solved an "urgent matter in December) to obtain an ex parte restraining order from this Court (Sanko Steamship Co. Ltd. v. Newfoundland Refining Company Limited et al, 76 Civ. 756) against, among others, PRC, which contained, inter alia, the following restraining order:

> "ORDERED that the Sumitomo Bank, Ltd...be temporarily restrained from removing or releasing up to an amount of $3,000,000 which said banks may be holding for defendants in any manner whatsoever including, but not linked [sic - limited?] to bank accounts and/or negotiable credits or securities which said banks are holding for the defendants."

In addition, a judgment against NRC, PRC and the other defendants was sought in the amount of over $8 million.

(38) On the same day, February 17, 1976, by agreement with NRC and PRC, Clarkson had taken over control of all cash receipts and disbursements of NRC and PRC, including the PRC bank account in Sumitomo.

(39) Thereafter on February 18, 1976, the Federal Court order was modified so as to permit disbursements by defendants "in the ordinary course of business", which disbursements were by then under control of Clarkson. But otherwise the TRO remained in effect. Since the only signing officers of PRC's account in

Sumitomo were Ataka employees, PRC could not withdraw funds therefrom "in the ordinary course of business" or otherwise, so the modification of the above quoted order had no effect upon the PRC account in Sumitomo.

(40) On the next day, with full knowledge of Clarkson, and in violation of both the order of the Newfoundland Court and the restraining order of this Court, Sumitomo took $905,739.52 from the PRC account claiming on PRC's bank statement that such was "partial Loan Repay 1205".

(41) While the PRC bank statements prepared by Sumitomo clearly state that the $2,637,926.85 taken from PRC's account on February 13, 1976, was "Partial Payment Loan 1204", and the $905,739.52 taken on February 20, 1976 was "Partial Loan Repay 1205", Sumitomo later, after being challenged for its actions in the state court action, belatedly produced a

long overdue bill of exchange drawn by Ataka on PRC which was on December 31, 1975, or January 30, 1976, illegally assigned to Atlantic by Ataka and which Sumitomo claimed had been assigned to it by Atlantic at some later date. Since none of the endorsements were dated, such allegation cannot be verified. Sumitomo claimed it had a right of "set off" against the bill of exchange, which it did not.

(42) The acts of Clarkson as a supposed disinterested fiduciary, or, more accurately, its lack of actions, speak far louder than words as to where its loyalty is and has been since it first entered this matter:

(a) In spite of the fact that the $3,500,000 payment from NRC to Sanko was a fraud on the PRC creditors, because PRC owed Sanko nothing, Clarkson has done nothing whatsoever to attempt to recover

that amount from Sanko for the benefit of PRC's creditors;

(b) In spite of the fact that the $3,000,000 letter of credit was drawn upon by Ataka in express violation of the solemn undertaking of Ataka's managing director, Clarkson has taken no action to recover that amount for the benefit of the PRC creditors;

(c) In spite of the fact that Sumitomo has taken $3,426,663.37, which was in Clarkson's constructive custody, in violation of the order which Sumitomo, through Atlantic, caused to be issued by the Newfoundland Court, and in spite of the fact that $905,739.52 thereof was taken in violation of the restraining order of this Court, procurred by Sumitomo through Sanko, and in spite of the fact that such is clearly an unlawful preference in favor of Sumitomo (Atlantic), Clarkson has done nothing to recover such sums for the

benefit of PRC's creditors.

It is also of considerable import that during the entire course of the proceedings in the Sanko case in this Court, the Court of Appeals, and while a petition for a Writ Certiorari was pending -- during which the Courts' restraining order, as modified, remained in effect --Sanko never made any effort to bring the $905,739.52 back under this Court's restraining order, and the attachment sought by Sanko. Nor did it ever try to force Sumitomo to refund the illegally taken $2,637,926.85 to be brought under the Court's restraining order. This is particularly interesting because that was the largest single bank account involved (all others combined were approximately $700,000).

(d) In spite of the fact that Ataka wrongfully took $18,000,000 of PRC's funds during the three months prior to the appointment of Clarkson as Interim Receiver,

thus obtaining an unlawful preference, Clarkson has done nothing to recover such money for the benefit of PRC's creditors;

(e) In spite of the fact that Sanko sought, in the case filed in this Court against PRC, and others, damages in excess of $8,000,000, and in spite of the fact that there was no reason whatever for Sanko to assert such a claim against PRC, and in spite of the fact that if judgment in such amount was for any reason recovered against PRC, it would have further reduced the amount available for PRC's valid creditors, Clarkson made no effort to assist in the defense of that action, though it was fully appraised thereof;

(f) Last but by no means least, Clarkson has made no effort whatsoever to force Atlantic, as assignee of the Agency Agreement, or Ataka as the assignor, to continue to perform that Agreement in the manner Ataka had, by two years of

practical construction, admitted it was bound to do, i.e., continue to provide financing required for purchase of crude oil required by the refinery. Certainly where the parties had agreed that when the rights and obligations thereunder were disputed -- as they clearly were -- the matter was to be submitted to a New York Court, Clarkson was bound, as a disinterested fiduciary, to seek such a determination in accordance with the contract, not simply let Ataka "off the hook" unilaterally. The other creditors of NRC and PRC had a vital interest in that Agency Agreement. If Ataka had continued to permorm as it had admitted it was bound to do, by practical construction of the contract for two years, the PRC refinery would not have been shut down and 500 people put out of work.

WHEREFORE defendants demand judgment vacating the preliminary injunction of this

Court dated April 1, 1976 ordering the plaintiff forthwith to return all documents taken by plaintiff from NRC and PRC to the location from which they were taken, denying the relief sought in the complaint and awarding defendants the costs of this action.

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EXCERPTS FROM PETITIONER'S
ANSWER AND COUNTERCLAIM BELOW

[Initial portions of Answer
and Counterclaim are Omitted]

(15) By an "Agency Agreement", dated September 20, 1973, between NRC as principal and as agent of PRC, Ataka Japan, and Ataka America:

(a) Ataka was appointed by NRC "as its exclusive purchase and sales agent for ALL THE CRUDE OIL contracted by NRC with its suppliers to sell to [PRC]..."; and Ataka agreed to purchase all crude oil contracted for by NRC in accordance with the terms of the BP Trading contract, including the furnishing of letters of Credit required under the said BP Trading contract, for which Ataka was to be paid a commission on all such purchases;

(b) Ataka was to make payment for

all crude oil supplied to NRC, with NRC being responsible to Ataka for all of such payments in the manner hereinafter described;

(c) All sales of crude oil by NRC to PRC and receipts of payments therefor were to be executed by Ataka for and on behalf of NRC, with such funds being used by Ataka to pay the supplier of such crude oil;

(d) Ataka "as agent of NRC" agreed to extend to NRC credit facilities of Ataka for any advance to be made to NRC's crude oil supplier for the crude oil to be supplied to PRC, including Ataka's intention "to enable NRC to overcome start-up difficulties in the initial start-up stage until the refining operation has reached the normal scheduled production stage." For advances made by Ataka to NRC's crude oil supplier, NRC agreed to issue promissory notes to Ataka "according to the

repayment terms and conditions to be agreed...";

(e) The parties agreed that such agreement would continue in effect for at least ten years or until all indebtedness of NRC to Ataka had been repaid, whichever was longer.

(16) The Agency Agreement contained the following provision:

> "This agreement shall be construed in accordance with the laws of the State of New York and any dispute arising between the parties shall be submitted for determination by a New York Court." (Emphasis added)

(17) (a) By separate Supplementary Agreement, dated September 20, 1973, Ataka agreed to a loan of $42,000,000 to NRC; such loan was to be represented by NRC's unsecured promissory notes maturing June 30, 1985, this Agreement incorporated by reference inter alia the above quoted forum selection clause. By agreement with Ataka, NRC was to use such funds to further

its efforts, through affiliated companies of NRC and defendant John Shaheen, to expand into other enterprises in which Ataka and such affiliated companies could expand their economic interests;

(b) By a separate Loan Agreement dated November 17, 1972, Ataka loaned PRC secured by a First Mortgage on the refinery. That Agreement provided:

> "14(a). This Agreement shall be construed and the relations among the parties with respect hereto shall be determined in accordance with the laws of the State of New York."

(18) The PRC refinery was partially completed in December 1973, in substantial breach of the contractual commitment of the construction contractor to complete it early in 1973; many portions of the plant were not completed. Attempted start-up disclosed many design and construction errors which have prevented completion and

acceptance up to the present time. NRC and PRC have instituted a civil action in the Supreme Court of New York County for $189,000,000 in damages against UOP, Inc., the company which designed most of the refinery, and its wholly-owned subsidiaries, Procon, Inc. and Procon (Great Britain) Ltd. which constructed the refinery.

(19) On January 18, 1974, in a premature effort to invoke the provisions of Article III(a) of the Agency Agreement under which PRC was obligated to increase its $3,000,000 Letter of Credit after 18 months to an amount "equal to the average of the cost of the shipments of the last three (3) months", Ataka suggested that the said Letter of Credit be increased to a higher level required because of the increased cost of crude oil. M. Takagi, Managing Director of Ataka, "guaranteed" that the Letter would "not be used and in case of

need I will work out with you some other method of refinancing should instances occur." Nothing more was done and the matter was dropped until August 1975, when Ataka suggested an increase in the Letter of Credit to approximately $22,500,000. After some discussion the matter was dropped. No default was ever called by Ataka under this provision.

(20) On October 16, 1974, the first Bill of Exchange which PRC did not have funds to pay became due; in accordance with the understood payment procedure, Ataka caused such Bill of Exchange, which was in the amount of $15,400,000, to be "rolled over" to December 15, 1974. Ataka paid that Bill of Exchange on the due date and PRC reimbursed Ataka on December 16th and 17th; thereafter, on 19 spearate occasions Bills of Exchange were "rolled over" or "re-rolled over" to conform to the ability of

PRC to pay such Bills of Exchange. Until February 13, 1976, no payment obligation of PRC or NRC was ever demanded unless adequate funds were available for payment thereof.

(21) In February 1975, Ataka began efforts to have its then unsecured claims against NRC and PRC secured by a Third Mortgage on the refinery, on the representation that such a third mortgage was being required by Ataka's bank, which, on information and belief, was defendant Sumitomo. Even though the Agency Agreement made no provision for such third mortgage, NRC and PRC undertook to endeavor to obtain the consent therefor from the holders of the First and Second Mortgages.

(22) While negotiations were in progress with respect to a third mortgage security for Ataka's claim, the First National Bank of Chicago ("Chicago Bank"), a creditor

of PRC in the amount of approximately $28,000,000, of which $20,000,000 was secured by a debenture with a lien on the crude oil and product inventory of PRC, caused a Receiver to be appointed by the Newfoundland courts on October 24, 1975, on the basis of a default in payment which was then due.

(23) Ataka then caused meetings to be held among Ataka, UOP, Inc. (which, as indicated in paragraph 18 hereof, designed a large part of the refinery and the parent company of the contractor which constructed the refinery), NRC, PRC and certain affiliated interests. As a result of such meetings, an agreement dated October 28, 1975, was executed among said parties providing, inter alia:

(a) the effective date of said agreement was to be when the holders of the first and second mortgages granted their

consent to the issuance of a third mortgage;

(b) immediately upon execution of the agreement, a number of steps were to be taken for Ataka and UOP to take over effective control of the management of NRC, PRC and certain of their affiliates;

(c) Ataka and UOP would undertake through financial support (without any obligation to supply additional funds) and otherwise, including management of the operations, to use their "best efforts to continue the operations of PRC with the right to terminate such support in the event they decide they are unable to continue such operations on a profitable basis."

(24) UOP failed to take any action with respect to the October 28, 1975 Agreement; in spite of the fact that certain parts of the Agreement were not performed, the financial and accounting management

of NRC and PRC were isolated and placed under the control of Ataka in accordance with the said Agreement. Office space was provided Ataka and its accountants and all financial decisions and receipts and payments of all types were placed under their absolute control and discretion. From that time forward until February 13, 1976, the affairs of NRC and PRC remained under the control of Ataka, which was then under control of Sumitomo Bank.

(25) Following the assumption of control of the affairs of NRC and PRC, Ataka

(a) On November 8, 1975, paid the then remaining $18,000,000 owed to the Chicago Bank by PRC (said amount having been reduced by $10,000,000 from proceeds of accounts receivable seized by the Chicago Bank); Ataka requested as part of the transaction a demand debenture of PRC ("First Debenture") secured by a lien on PRC's

crude oil and refined product inventory. It was understood by PRC and NRC that this note would remain outstanding as were the Bills of Exchange.

(b) "Rolled over" a Bill of Exchange for $18,700,000, due on November 11, 1975, to November 9, 1976, for one year, and Bills of Exchange for $11,200,000 and $9,700,000 due, respectively, on November 26th and 29th, 1975, to January 26th and 30th, 1976, based upon Ataka's decision as to the then projected cash flow of PRC which showed that two Bills of Exchange could be paid on those dates, without interference with the normal conduct of PRC's business.

(c) for the first time, altered the procedure for payment for crude oil; Ataka loaned $25,000,000 to PRC on December 15, 1975, which Ataka then took back to pay itself for a cargo of crude delivered to PRC; Ataka required another debenture ("Second

Debenture"), secured as described in subparagraph (a) above and due February 15, 1976; all in fraud of the PRC creditors and in violation of the Agency Agreement. It was understood by NRC and PRC, who had no suspicion of the ulterior motive involved in this transaction, that they would be "rolled over" as were the Bills of Exchange to coincide with PRC's cash flow.

(d) On December 23, 1975, drew against the $3,000,000 Letter of Credit which had been outstanding and untouched since September 13, 1973, in violation of Ataka's "promise" never so to do.

(e) in accordance with the newly instituted procedure, advanced $6,320,000 to PRC on January 30, 1976, which was used for a similar purpose as described in (b) above, with the issuance of a third debenture (Third Debenture") due May 1, 1976; again in fraud of the PRC creditors and in violation of the Agency Agreement. It was

similarly understood by NRC and PRC that these maturities would be "rolled over" as were the Bills of Exchange.

(26) On or about November 15, 1975, Sumitomo Bank, Ataka's principal Japanese bank, began to exert its influence in the conduct of the relations between Ataka, NRC and PRC; shortly thereafter, on or about December 15, 1975, Morgan, Stanley, investment bankers, was retained, either by Sumitomo Bank acting on behalf of Ataka, or directly by Sumitomo Bank, to give advice on the future conduct of the relationships between Ataka, PRC, NRC and, apparently, on the relationships with the other Shaheen companies (i.e., subsidiaries of John Shaheen).

(27) On information and belief, the handling of all of Ataka's relationships with NRC, PRC and the other Shaheen companies was placed under the control of

Morgan Stanley on or about December 15, 1975. Within days of the retention of Morgan Stanley, the cordial and cooperative relationships between Ataka and the Shaheen companies terminated.

(28) As indicated in paragraph 25(c) above, Ataka, on November 15, 1975, for the first time, changed the payment procedures set forth in the Agency Agreement which had been followed for two years and involved credit advances by Ataka to NRC and PRC of more than $490,000,000 in 1974 and 1975. Ataka required the issuance of the Second and Third Debentures. It was this change in the payment procedure, coupled with subsequent actions by Ataka and Sumitomo Bank in connection with the Second Debenture, which constituted a substantial breach of the Agency Agreement and the perpetration of unlawful conversion of the funds of PRC and NRC by Ataka and Sumitomo Bank.

(29) Between December 29, 1975 and February 10, 1976, Ataka and Sumitomo Bank:

(a) unlawfully converted to their own use $18,700,000 of PRC's operating funds;

(b) acting in concert with Sanko Steamship Company, of which Sumitomo Bank is a principal bank, unlawfully forced PRC to pay, for account of NRC, $3,500,000 of funds for charter hire of vessels chartered to NRC, and which NRC would not otherwise have paid as not being due and owing.

(30) Thereafter, on February 13, 1976, the day Ataka moved for the appointment of defendant Clarkson as Receiver by the Newfoundland Court by alleging the insolvency of NRC and PRC, as is more fully described in the following paragraph and, the Sumitomo Bank, without prior notice to PRC of any claimed amount due Sumotomo Bank, unlawfully converted to its own use,

$2,637,929 of PRC's funds, claiming a right of "set off." Thereafter, on February 20, 1976, a customer paid $905,739 into PRC's Sumitomo Bank account, following previous instructions given by PRC, and Sumitomo Bank immediately and unlawfully converted said amount to its own use, again claiming a "set off."

(31) On February 13, 1976, Morgan Stanley, acting for Summitomo Bank, Ataka and Atlantic Trading, pursuant to a definite plan entitled "Project Winnet", caused Atlantic Trading, in violation of the Agency Agreement, to claim defaults on the First, Second and Third Debentures and on the basis of such alleged defaults, Atlantic Trading, on February 13, 1976, (a) appointed Clarkson Receiver of the inventory purportedly under liens securing

the said Three Debentures; (b) requested and obtained the ex parte appointment of Clarkson as Receiver of all the assets of NRC and PRC by the Supreme Court of Newfoundland. In the document filed with the Newfoundland Court in support of its application for the appointment of Clarkson as Interim Receiver, Atlantic Trading made many false and fraudulent allegations, and failed to make material disclosures; had such false and fraudulent statements not been made and had the material omissions been disclosed, no legal grounds for the appointment of the Receivers would have existed. Atlantic Trading also failed to disclose to the Newfoundland Court that (a) the reason why NRC and PRC were not meeting their current obligations to other creditors was that, between November 15, 1975 and February 13, 1976, Ataka and Sumitomo Bank had unlawfully converted approximately $28,000,000 of the funds of

NRC and PRC for their own use, and (b) Ataka had breached the Agency Agreement including the existence of the New York "forum slection" caluse in the Agency Agreement.

D. SECOND COUNTERCLAIM

(32) Counterclaim plaintiffs repeat and reallege paragraphs 1 through 31 in their entirely with the same force and effect as if they were herein repeated in full.

(33) Counterclaim defendants, acting in concert, caused Ataka substantially to breach the Agency Agreement in that Ataka

(a) forced PRC to issue the First, Second, and Third Debentures, dated, respectively, November 8, 1975, December 15, 1975 and January 30, 1976.

(b) wrongfully converted the amount of $18,700,000 of the operating funds of PRC and NRC.

(c) breached the Agency Agreement providing for the arrangements for the

financing of the purchase of crude oil necessary for the operation of the refinery for which Ataka was the "sole agent" and thus forced the shutdown of said refiner.

(d) by the illegal assignment of the Ataka claims to Atlantic Trading, caused Atlantic Trading to invoke the jurisdiction of the Bankruptcy Court of Newfoundland on the falsely alleged bankruptcy of NRC and PRC, all in violation of the Agency Agreement's designation of the New York Courts as the proper form for determination of disputes under the Agency Agreement and Supplemental Agreement all causing irreparable injury and damage to PRC, NRC and counterclaim plaintiff's investment therein.

E. THIRD COUNTERCLAIM

(34) Counterclaim plaintiffs repeat and reallege paragraphs 1 through 33 in their entirety with the same force and effect as if they were herein repeated in full.

(35) Counterclaim defendants, acting in concert, caused Atlantic Trading to wrongfully invoke the jurisdiction of the Supreme Court of Newfoundland and caused the appointment of a Receiver of NRC and PRC based upon false and fraudulent representations to the said Court, causing irreparable injury and damage to NRC, and PRC and counterclaim plaintiffs' investment therein.

F. FOURTH COUNTERCLAIM

(36) Counterclaim plaintiffs repeat and reallege paragraphs 1 through 35 in their entirety with the same force and effect as if they were herein repeated in full.

(37) Counterclaim defendants, acting in concert, caused Atlantic Trading to wrongfully invoke the jurisdiction of the Newfoundland Court, which resulted in the wrongful appointment of Receivers of NRC and PRC's assets, and caused a default to be

declared by certain holders of the First and Second Mortgages on the refinery, which in turn, resulted in those creditors appointing Clarkson as Receiver of the refinery, and Clakson, acting on the instructions of counterclaim defendants, shut down the refinery and discharged most operating personnel, all causing irreparable damage to NRC, PRC and counterclaim plaintiffs' investment therein.

G. FIFTH COUNTERCLAIM

(38) Counterclaim plaintiffs repeat and reallege paragraphs 1 through 37 in their entirety with the same force and effect as if they were herein repeated in full.

(39) Defendant Sumitomo Bank wrongfully converted to its own use $3,543,666 of the funds of NRC and PRC, and tortiously interfered in the contractual relations between NRC and PRC and Ataka, and caused Ataka to breach the Agency Agreement with NRC

and PRC and counterclaim plaintiffs' investment therein.

H. SIXTH COUNTERCLAIM

(40) Counterclaim plaintiffs repeat and reallege paragraphs 1 through 39 in their entirety with the same force and effect as if they were herein repeated in full.

(41) Defendants Ataka and Sumitomo Bank, together with Sanko Steamship Company, acting in concert, caused the wrongful payment of $3,500,000 of PRC's funds to Sanko Steamship Company, to which PRC owed nothing, all causing irreparable injury and damage to NRC, PRC and counterclaim plaintiffs' investment therein.

I. SEVENTH COUNTERCLAIM

(42) Counterclaim plaintiffs repeat and reallege paragraphs 1 through 41 in their entirety with the same force and effect as if they were herein repeated in full.

(43) All of the defendants and Sanko Steamship Company, acting in concert and

under the direction and control of defendant Morgan, Stanley and its attorneys, entered into and actively participated in a conspiracy, for the purpose of breaching the Agency Agreement, wrongfully invoking the jurisdiction of the Supreme Court of Newfoundland, wrongfully causing a Receiver to be appointed, wrongfully converting funds of NRC and PRC and causing wrongful payments of funds of NRC and PRC, and said counterclaim defendants and Sanko did in fact breach said Agency Agreement, wrongfully invoke the jurisdiction of the Supreme Court of Newfoundland, wrongfully cause a Receiver to be appointed, wrongfully convert funds of NRC and PRC, and caused wrongful payment of funds of NRC and PRC as described in Claims First through Fifth hereof, and Sanko wrongfully sought to attach all of the bank accounts of NRC, PRC and four of their affiliates.

(44) In furtherance of said conspiracy, all the defendants performed, among others, the following acts:

(a) wrongfully, and using extreme eonomic duress, in violation of the Agency Agreement, caused Ataka to demand that PRC execute and deliver to Ataka the First, Second and Third Debentures;

(b) wrongfully deprived NRC and PRC, during the period November 15, 1975 through February 10, 1976, of $25,200,000, $18,200,000 of which was wrongfully converted by Ataka to its own use; $3,500,000 of which was wrongfully converted by Sumitomo Bank to its own use and $3,500,000 of which was wrongfully diverted to Sanko to its own use, all with the objective and purpose of making NRC and PRC insolvent and unable to pay the claims of its creditors as they became due, as part of the overall objective to put NRC and PRC in bankruptcy;

(c) On or before February 6, 1976, caused Atlantic Trading wrongfully, and in violation of Section 489 of the Judiciary Law of New York to accept the assignment from Ataka America of all of the assets and liabilities arising out of or relating to the dealings between Ataka America and Ataka Japan and NRC and PRC, for the purpose of bringing the bankruptcy action and furthering the objectives of the conspiracy alleged herein.

(d) On February 13, 1976, caused Atlantic Trading, as Ataka's assignee in violation of the New York Judiciary Law, Section 489, to demand payment of $18,000,000 from PRC, which, by reason of the Agency Agreement, was not then due and payable, with full knowledge that the wrongful diversion of PRC's funds by defendants had rendered PRC unable to pay said amount; on the same day, and using PRC's alleged inability to pay said First Debenture as a basis therefor, defendants caused Atlantic Trading to

(i) invoke the default clauses under the First, Second and Third Debentures;

(ii) appoint Clarkson as receiver and manager of the property secured under said First, Second and Third Debentures and instructed Clarkson to take immediate possession thereof which Clarkson did with full knowledge of the existence and objective of the conspiracy.

(iii) file a false and fraudulent Application, supported by false and fraudulent affidavits, with the Supreme Court of Newfoundland for the appointment of Clarkson as an Interim Receiver under the Bankruptcy Act of Newfoundland for the purpose of taking immediate possession of all assets of PRC and NRC and to control its receipts and disbursements and authorizing Clarkson to institute "such legal proceedings in Canada and in any other jurisdiction as may be advisable to conserve the property of" NRC and PRC.

(e) Sanko, on February 17, 1976, as part of the conspiracy, wrongfully attached the New York bank accounts of NRC and PRC and four of their affiliates which had no dealings with Sanko whatsoever.

(45) By reason of the foregoing, counterclaim plaintiffs have suffered damages to their investments in NRC and PRC in the amount of $100,000,000, and other irreparable damages.

J. EIGHTH COUNTERCLAIM

Counterclaim plaintiffs, in their respective individual capacities as employees of NRC and PRC, on their own behalf and for and on behalf of all members of the class consisting of former employees of NRC and PRC who lost their employment on or after February 13, 1976, by reason of the events described herein, counterclaim against Clarkson, as Trustee, and complain of counterclaim defendants as follows:

1. The allegations of the First through the Seventh Counterclaims above, are repeated and realleged as if repeated in full herein, except for paragraphs (1) and (2), and except as said paragraphs refer to damage to counterclaim plaintiff's investments in NRC and PRC.

2. Plaintiff Clarkson and counterclaim defendants, acting in concert conspired to and did deprive all members of said class of their jobs and livelihoods and thus caused damage to each and every member in an amount not yet fully ascertainable, but to date equal to several months pay which, as each month passes, increases the damage to each.

3. The suffering and deprivation caused to the members of the class has been tremendous, all caused by the deliberate acts of counterclaim defendants without regard to any member of the class but solely directed to wrongful objectives of the counterclaim defendants as described herein.

PRAYER FOR RELIEF

1. Defendants demand judgment dismissing the complaint together with the costs and disbursements of this action.

2. Counterclaim plaintiffs demand judgment as follows:

A. On the first counterclaim

(i) permanently enjoining counterclaim defendant Atlantic Trading from asserting any claims assigned to it by Ataka America in any action or proceeding anywhere in the world.

(ii) directing counterclaim defendants Ataka Japan and Ataka America to specifically perform the Agency Agreement with NRC and PRC.

B. On the second counterclaim, against counterclaim defendants Ataka Japan and Ataka America in the sum of $100,000,000.

C. On the third counterclaim, against counterclaim defendants Ataka Japan and Ataka America in the sum of $100,000,000.

D. On the fourth counterclaim, against counterclaim defendants Ataka Japan and Ataka America in the sum of $300,000,000.

E. On the fifth counterclaim, against counterclaim defendant The Sumitomo Bank Ltd. in the sum of $3,543,666.

F. On the sixth counterclaim, against counterclaim defendants Ataka Japan, Ataka America and Sumitomo Bank, in the sum of $3,500,000.

G. On the seventh counterclaim, against all counterclaim defendants, in the sum of $100,000,000.

H. On the eighth counterclaim, against all counterclaim defendants in the sum of $50,000,000.

I. Granting such other and further relief to the counterclaim plaintiffs as the Court may deem just and proper.

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APPENDIX D

DECISION OF THE COURT OF APPEALS FOR THE SECOND CIRCUIT, OF WHICH REVIEW IS SOUGHT

UNITED STATES COURT OF APPEALS

FOR THE SECOND CIRCUIT

No. 765-7, 778 September Term, 1980

Argued: April 20, 1981 Decided: September 15, 1981

Docket Nos. 80-7664, 80-7712, 80-7754, 80-7790

THE CLARKSON COMPANY LIMITED, as Trustee in Bankruptcy, appointed by the Supreme Court of the Province of Newfoundland, of the property of Newfoundland Refining Company Limited and Provincial Refining Company Limited,

Plaintiff-Appellee,

-against-

JOHN M. SHAHEEN, ROY M. FURMARK, ALBIN W. SMITH, PETER L. CARAS, PAUL W. RISHELL, SHAHEEN NATURAL RESOURCES COMPANY, INC., NEWFOUNDLAND REFINING COMPANY LTD., U.S.A. and FOUNDERS CORPORATION,

Defendants-Appellants,

PHILIP GANDERT, WILLIAM J. SHERIDAN,

Defendants.

DONALD B. DaPARMA, ESQ., New York, N.Y. (Breed, Abbott & Morgan, New York, N.Y., Robert Ferri, Esq., of counsel), for Defendant-Appellant, Roy M. Furmark.

LOLA S. LEA, ESQ., New York, N.Y., for Defendants-Appellants Albin W. Smith, Paul W. Rishell, and Peter L. Caras

JEFFREY BARIST, ESQ., New York, N.Y. (White & Case, New York, N.Y., Edna R. Sussman, Esq., Kevin D. Ashley, Esq., of counsel), for Plaintiff-Appellee.

Before: LUMBARD and MESKILL, Circuit Judges, and MacMAHON, District Judges, and MacMAHON, District Judge.*

Appeal from a judgment of the United States District Court for the Southern District of New York, Owen, J., ordering corporate defendants to repay loans to the trustee in bankruptcy and awarding damages against director defendants for breach of their fiduciary duty to the creditors.

Affirmed; judgment amended.

THOMAS A. ANDREWS, ESQ., New York, N.Y. (Saxe, Bacon & Bolan, P.C. New York, N.Y., Howard F. Husum, Esq., Filip L. Tiffenberg, Esq., of counsel), for Defendants-Appellants John M. Shaheen, Shaheen Natural Resources Company, Inc., Newfoundland Refining Company Ltd., U.S.A., and Founders Corporation.

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* Honorable Lloyd F. MacMahon, of the United States District Court for the Southern District of New York sitting by designation.

LUMBARD, Circuit Judge:

This is an appeal from a judgment won in the Southern District of New York by The Clarkson Company Limited, the Newfoundland trustee in bankruptcy of Newfoundland Refining Company Limited (NRC), suing in diversity jurisdiction to recover monies advanced or loaned by NRC to John Shaheen and companies controlled by him (the Shaheen group), and to recover damages from five individual directors of NRC for causing such loans to be made. At trial, the jury found that Shaheen and his companies owed a total of $50 million to NRC; of this, $30 million, consisting of loans made by NRC to the Shaheen group during 1974 and 1975, was advanced when NRC was insolvent, without fair consideration, and hence was fraudulent to creditors and in violation of sections 273 and 274 of the New York Debtor and Creditor Law. A Promissory Note and Letter Agreement executed

in October, 1975 was found fraudulent for the same reasons. The judgment ordered the Shaheen group to repay the $50 million in loans; held the five directors jointly and severally liable with the Shaheen group for the $30 million fraudulently loaned in 1974 and 1975; held the five directors jointly and severally liable for the $23 million in damages caused by entering into the Promissory Note; and declared the Promissory Note null and void. The $30 million sum assessed against the directors for breach of the fiduciary duty owed to creditors was apportioned according to the percentage amounts assigned by the jury against each.[1/]

The defendants allege numerous errors, chiefly the insufficiency of the evidence to support the verdict, and numerous rulings by the district court in the exclusion of evidence and the charge to

the jury. Most of these contentions are disposed of by consideration of the evidence, which we find amply supported the verdicts. However, we find unjustified on this record the unapportioned liability of the individual directors for the $23 million damages on the Promissory Note. We hold that that amount must also be apportioned in the same percentages as determined by the jury for the $30 million advanced during 1974 and 1975. In all other respects, the judgment is affirmed.

In 1968, Newfoundland Refining Company Limited was organized under the laws of the Province of Newfoundland to build and operate an oil refinery at Come-By-Chance, Newfoundland. Title to the refinery was in Provincial Refining Company, Ltd. (PRC), a joint venture of NRC and the Newfoundland Government, and NRC was to construct and operate the refinery. NRC was part of a complex of

corporations directly or indirectly controlled by John Shaheen; its books and records were kept in Shaheen's New York City headquarters.

On March 12, 1976, NRC and PRC were found to be bankrupt by the Chief Justice of Newfoundland, who presided over a week-long hearing. During that hearing, the Shaheen group contested the bankruptcy petition filed by an assignee of Ataka America, Inc., the Japanese controlled organization that had advanced to NRC part of the money to build and operate the refinery.[2/] The Clarkson Company was appointed trustee and the Supreme Court of Canada affirmed. Both during and after this proceeding, the Shaheen group sued in the federal and state courts in New York attacking the Canadian bankruptcy adjudication and, later, Clarkson's performance as trustee. These suits were all

dismissed.[3]

When Shaheen denied Clarkson access to, and possession of, the records of the bankrupt companies, Clarkson brought suit in the Southern District to compel delivery of the records. Judge Owen granted Clarkson a preliminary injunction and we affirmed, 544 F.2d 624 (1976). As to Shaheen's attack on the Canadian proceedings, we found that Shaheen had "not shown enough at this stage to cast doubt on the Canadian judgment." Clarkson then moved to amend its complaint to add the claims regarding monies advanced to the Shaheen group and to add as defendants three additional recipients of monies advanced by the bankrupts.

The district court granted Clarkson's motion to amend the complaint, and granted a permanent injundction giving Clarkson the NRC and PRC records. It also denied the Shaheen motion to amend the

answer to include charges of fraud in the procurement of the Newfoundland bankruptcy. Judge Owen held that the proposed amended answer, asserting allegations of wrongdoing "on information and belief" without stating any factual basis for the allegation, did not conform to the pleading requirements of Fed.R.Civ.P. 9(b), and that the acts alleged as constituting the "fraud" had either been "rejected time and time again" or related to Clarkson's conduct as trustee and were irrelevant to the claim of a fraudulent appointment. Later, Judge Owen struck from the Shaheen answer to Clarkson's amended complaint similar allegations of fraud asserted to contest Clarkson's standing. The Shaheen defendants attack these orders on this appeal.

At the trial in June, 1980, the evidence regarding moneys advanced to the Sheehan group was virtually undisputed.

From 1972 until bankruptcy in March, 1976, NRC's books showed that it loaned over $51 million to Shaheen and Shaheen controlled corporations.

John M. Shaheen	$ 501,231
Shaheen National Resources Company, Inc. (SNR)	46,049,040
Newfoundland Refining Company, Ltd., U.S.A. (NRC, Ltd. U.S.A.)	2,344,268
Founders	548,392
Newfoundland Pulp & Chemical Co. Limited	2,156,952
Canadian Caribbean Oil Co. Limited	145,747
Shaheen Natural Resources Co. Limited	265,012

The individual defendants, Shaheen, Furmark, Smith, Caras and Rishell, were directors of NRC and various other Shaheen companies at the time of the loans. Furmark was Vice Chairman of the Board of Directors, Executive Vice President and Treasurer of NRC, and Smith, Caras and Fishell were

directors and officers of NRC, from at least 1972 to the bankruptcy in March 1976. Each of these defendants also served as officers and directors of other Shaheen related companies, including corporations which were the recipients of funds from NRC. Of the six Shaheen corporations to which NRC loaned money, Shaheen was a director and controlling person of each; Furmark was an officer and director of each; and Caras an officer or director of five.

The loans made during 1974 and 1975 were made at the direction of Shaheen or Furmark or both Shaheen and Furmark, according to Caras, Furmark, Caras and Smith each participated in the making of the loans by signing checks. Caras, who signed checks for over $9 million in loans, testified that he did not know the purpose of a single payment for which he signed checks, either at the time he signed them or thereafter.

Caras and Rishell, both directors of NRC, could not recall attending any meetings of the NRC Board, receiving any minutes of Board Meetings, reviewing any financial information, knowing that NRC had made loans to any other Shaheen company, or making any inquiry as to the use of the funds that NRC was lending to Shaheen and his other companies.

The loans were recorded on the books of NRC as an "open account." Clarkson contended that the loans when made were due on demand, as evidenced by the fact that they were carried on the books of NRC without due date, and that NRC's outside auditors, Coopers & Lybrand, and NRC's internal accounting staff understood the loans to be due on demand.

In October 1975 Shaheen and Furmark directed that the debts owing from Shaheen and his corporation to NRC be reset

to be due in 1985 by means of a Letter Agreement between NRC to SNR, a Promissory Note, and a letter from MRC to SNR, all dated October 27, 1975. According to the Letter Agreement, all open account indebtedness owing to NRC from 29 Shaheen affiliates, including the defendant corporations, and from seven individuals, including Shaheen, Furmark, Caras and Rishell, was cancelled in exchange for SNR's promise on behalf of the others to enter into a promissory note for the total amount due, at 6% interest per annum, with payment of interest and principal deferred until June 30, 1985. By letter of the same date NRC requested SNR to have the SNR debt stated in a promissory note. The Promissory Note, also dated October 27, 1975, purports to restate SNR's indebtedness to NRC, is in the amount of $45,481,076, at 6% interest per annum, interest and principal due on June 30, 1985, and states that

it is to be construed in harmony with the Letter Agreement. The Letter Agreement, the Promissory Note and the Letter were purportedly signed by Caras on behalf of SNR. Caras admitted his signature, but said that he had no recollection of the transaction or even of having signed the documents. Shaheen and Furmark testified that the Promissory Note merely memorialized the pre-existing intention of all the parties and that they directed the roll-over on October 27 because they were about to turn over control of NRC to its creditors. On October 23, 1975, the First National Bank of Chicago claimed default on notes of PRC aggregating $28,000,000. NRC, PRC's parent, was then insolvent according to an internally prepared financial statement at June 30, 1975. Thereafter, negotiations were conducted among creditors of NRC and PRC and the Shaheen interests to restructure the debts of NRC and PRC, ultimately

resulting in a draft agreement dated October 28, 1975, which provided for creditor control of NRC. In an affidavit Furmark explained that the October 1975 agreement contemplated that creditors "would have assumed effective control" of NRC and that "in view of the impending transfer of control of" NRC "I concluded that it would be desirable to reset the obligations of Shaheen Natural Resources Company, Inc. to Newfoundland Refining Company Limited...on a long-term basis...." The books and records of NRC did not disclose that NRC received any consideration or benefit, or that any business purpose of NRC was served by the loans or the roll-over.

The court put ten special questions to the jury, the pertinent answers to which may be summarized as follows:

1. The loans to the defendants that were unpaid as of March 13, 1976 were:

John M. Shaheen	$ 501,231
SNR	46,049,040
NRC, Ltd. U.S.A.	2,344,268
Founders Corp.	548,392

2. The loans to the defendants were due on demand and not in 1985 as the defendants claimed.

3. In 1974 and 1975 NRC was insolvent and the $30 million in loans made in those years violated sections 273 and 274 of the New York Debtor and Creditor Law.

4. In October 1975, at the time of the Promissory Note and Letter Agreement, NRC was insolvent. The Promissory Note and Letter Agreement violated sections 273, 274 and 276 of the New York Debtor and Creditor Law.

Immediately after receiving the jury verdict, Judge Owen who sat simultaneously as an equity judge on the claim to invalidate the Promissory Note of October, 1975, held the note to be a nullity on the

basis of similar findings:

> [T]he intention of the parties at the outset of these advances was that they be due upon demand... as of October 1975 NRC was insolvent and ... the note and related papers that were issued at the same time were a fraudulent conveyance without consideration with intent to hinder, delay and defraud creditors....

The jury also found that the five individual defendants had breached their fiduciary duty to NRC and its creditors with respect to (a) the making of loans and advances in 1974 and 1975, and (b) the making of the Promissory Note of October 1975.

Of the $30,609,026 advanced in 1974 and 1975, the jury found that damage had been caused by the individual defendants in the following percentages of that amount:

Shaheen	74%
Furmark	20
Smith	2
Caras	2
Rishell	2

Counsel had already stipulated that, if the jury found liability on the Promissory Note, the damages were $23,073,792 (the unpaid interest, computed at 6%, on the principal amount of the Note from March, 1976 to the date of judgment). Judgment was thereafter entered on July 22, 1980 and a motion of the director defendants for judgment n.o.v. was denied. This appeal followed.

THE COURT'S CHARGE

We find no error in the court's charge, Although the court first charged that the mere fact that inter-company advances were carried on an open account established that they were due on demand, this was later corrected to make it clear that it was for the jury to decide whether such loans were due on demand. Defendants' counsel expressed satisfaction with this correction.

The director defendants claim reversible error in the court's charge with respect

to their liability for breach of their fiduciary duties to the creditors.[4/] We disagree. Judge Owen charged that directors have an affirmative duty to inform themselves about the affairs of the corporation. He coupled with that a limitation of that duty to the effect that a director may rely on information, opinions, reports or statements including financial data prepared by persons regarding matters which the director believes to be within the competence of such persons as long as the director is acting in good faith and with care in so doing, reading from section 717 of the New York Business Corporation Law. The court emphasized that liability of the directors must be based on a finding that the directors knew or should have known of advances being made for less than a fair consideration while NRC was insolvent.

The defendants assert that under

New York law, a director's duty to the creditors arises not upon insolvency, but only when liquidation is "imminent and foreseeable." Defendants cite no New York cases for this proposition. We find the New York rule plainly stated in New York Credit Men's Adjustment Bureau, Inc. v. Weiss, 305 N.Y. 1, 7, 110 N.E. 2d 397 (1953), where the New York Court of Appeals held:

> If the corporation was insolvent at that time it is clear that defendants, as officers and directors thereof, were to be considered as through trustees of the property for the corporate-beneficiaries.

The defendants' claim that the duty of directors flows only to the corporation and not to the creditors "until it is clear that the corporation is no longer a going concern" flies in the face of the New York policy to preserve the assets of insolvent corporations for the creditors. See Ward v. City Trust Co. of New York, 192 N.Y. 61, 74, 84 N.E. 585, 589 (1908). Thus, the district court's charge was proper.[5/]

SUFFICIENCY OF THE EVIDENCE

The assertions of the individual defendants[6/] that the jury's verdict was not supported by the evidence is without merit. There was abundant evidence that NRC was hopelessly insolvent at the times in 1974 and 1975 when sums aggregating over $30 million were "loaned" to Shaheen and his controlled companies. The New York Debtor and Creditor Law Section 271 provides that a debtor is insolvent "when the present fair salable value of his assets is less than the amount that will be required to pay his future liability or his existing debts as they become absolute and matured." Here, the largest part of NRC's assets were receivables from NRC affiliates that were mostly uncollectible. Only if the jury was willing to accept expert testimony that the reproduction cost of the refinery was several hundred million dollars and that this was

an accurate measure of its "fair salable value" could the jury have found that NRC was not insolvent. The jury's common sense in rejecting such a distorted view is beyond question.

Likewise, there was sufficient evidence to support the finding that the directors knew or should have known that the "loans" were made when NRC was insolvent and without fair consideration. Furmark was the chief financial officer of NRC and actively participated in the challenged transactions. Clearly, the jury was entitle to find that he had actively breached the duty of due care owed to the creditors and had caused 24% of the damages. The jury's determination that each of the remaining directors was responsible for 2% of the damages is also supported by the evidence. These three defendants offered no evidence that they ever attempted to

inform themselves about the circumstances surrounding the loans, or that they relied in good faith on the statements of others. From these facts the jury could have rationally found a negligent breach of the duty of care owed to the creditors.

However, we find nothing in the record to support the different treatment of the director defendants with respect to the $30 million advanced in 1974 and 1975 and the $23 million in damages on the Promissory Note. Liability on the former was assessed and apportioned by the jury; the latter amount was stipulated by the parties and the court entered a judgment of joint and several liability without apportionment. Because the facts supporting liability for the $23 million were identical to those supporting liability for the $30 million, the court should have apportioned the damages in both cases. Consequently, we remand with instructions to modify the judgment to assess

liability against each defendant for the Promissory Note in the same proportions that the jury assessed liability on the $30 million in "loans."

RULINGS REGARDING ATAKA

Although Shaheen's brief gives a lengthy recital of Ataka's interest in NRC, and its relations with the Shaheen group, and claims error in the court's refusal to charge the jury that it could draw an inference favorable to the defense from Clarkson's failure to produce witnesses or documents from Ataka, we are not persuaded that this evidence was relevant to the issues before the jury -- namely, the circumstances of the advance of $30 million to Shaheen and the Shaheen group at times when NRC was insolvent. The defendants showed that Ataka was one of four lenders who provided financing for the construction of the refinery, Ataka advancing $15

million. [7] Later Ataka loaned NRC an additional $42 million. Ataka also committed itself to provide $300 million in financing to the Shaheen group. Thereafter, in 1976 Ataka initiated the bankruptcy proceedings in Newfoundland. Any evidence that Ataka might give with respect to the issues was equally available to the defendants and to Clarkson. During more than two years before trial no effort had been made by the defendants to make any such evidence available. Moreover, there was no showing that any evidence which might have been produced was in any respect relevant. The claims about fraud and conspiracy on the part of Ataka appear to have been nothing more than a smoke-screen, without any merit.

THE VERDICT AGAINST DIRECTORS

The appellants, Smith, Caras and Rishell argue that the verdict as to the $30 million in loans made while NRC was insolvent

cannot stand because it was a result of compromise and confusion. They claim that although the jury was charged as to joint and several liability of the directors, the verdict was rendered by apportioning the liability and finding these three directors each liable for 2%. Where, as here, the jury assessed damages in the total amount of $30 million, there was no compromise. There was simply an apportionment in accordance with the jury's assessment of the part played by each individual defendant in causing the damages. The court's handling of the damages to be assessed against the individual defenants, and the jury's response thereto, was certainly more favorable to each defendant than would have been the case had the assessment been joint and several. In any event, as the director defendants made no contention in the district court about the verdict being an improper compromise, we need not consider their claims here.

Caloagni v. Hudson Waterways Corp., 603 F.2d 1049 (2d Cir. 1979); Terkildsen v. Waters, 481 F.2d 201, 204-5 (2d Cir. 1973).

INVESTIGATION OF A JUROR

The appellants complain of the district court's refusal to permit investigation into possible prejudicial misrepresentations by a juror on voir dire. The juror disclosed during voir dire her employment by Credit Lyonnais Bank and that she was an officer. The court asked [illegible] jurors if any of them knew any of the defendants, and the failure of the jurors to respond indicated a negative answer. No further questions were asked regarding her employment at the bank. After the verdict, on July 25, 1980, Founders Corporation moved for a new trial, or in the alternative for a hearing to determine whether the juror made any misrepresentations on the voir dire. Judge Owen denied the motion and ordered that any inquiry

regarding the juror should cease.[8/] Obviously, the motion was based on pure speculation that the juror, a junior officer in the bank, would have known of Shaheen or any of the others. There was no reason to believe that the juror had not responded properly. Under all the circumstances Judge Owen acted properly in denying the motion and in censuring the parties in making such a flimsy claim.

The remaining claims of error merit only brief mention. The district court's denial of the Shaheen defendants' motion to amend their answer to assert unparticularized allegations of fraud in the Newfoundland bankruptcy proceeding and Clarkson's appointment was proper. Nor was there error in Judge Owen's ruling that the New York Banking Law did not prohibit a foreign trustee from bringing suit in New York.

The district court is directed to amend the judgment to assess liability for the $23 million damages on the Promissory Note in the same proportions that the jury assessed liability for the $30 million in loans made during NRC's insolvency. In all other respect, the judgment is affirmed.

Affirmed; judgment amended.

(continued on next page)

FOOTNOTES

1/ The $23 million in damages assessed against the individual directors for causing NRC to execute the Promissory Note was not apportioned.

2/ At the Canadian bankruptcy hearing, the Shaneen group charged that Ataka had conspired to force NRC into bankruptcy to avoid its commitment to provide additional financing for the troubled project. Shaheen also alleged that the assignment of Ataka's claims against NRC to the subsidiary that filed the bankruptcy petition was illegal and that Ataka had converted funds belonging to NRC and PRC. The Canadian court rejected all these claims.

3/ The first suit by the Shaheen group sought to enjoin Ataka and other creditors of NRC from participating in the bankruptcy proceeding, alleging that they had made fraudulent misrepresentations to

the Newfoundland Supreme Court to obtain the appointment of Clarkson as trustee. Plaintiffs voluntarily dismissed the suit after the federal judge held hearings but before a decision was rendered. Newfoundland Refining Company Limited and Provincial Refining Company Limited v. Ataka America, Inc., Ataka & Co., Ltd., Atlantic Trading (Delaware) Corp. and The Sumitomo Bank, Ltd., 76 Civ. 941 (D.D.N.Y. 1976). Plaintiffs then brought a similar suit in Supreme Court, New York County. SNR Holdings, Inc. as sole stockholder of Newfoundland Refining Company Limited and Provincial Refining Company Limited v. Ataka America, Inc., Ataka & Co., Ltd., Atlantic Trading (Delaware) Corp., The Sumitomo Bank Ltd., Morgan, Stanley & Co., Inc., Clarkson & Co. Limited, Clarkson, Gordon & Co., Kleinwort Benson Limited and the Government of the Province of Newfoundland and Labrador (Sup. Ct., N.Y. Co., Index

No. 03959/1976). The judge denied the motion for a preliminary injunction and the Appellate Division affirmed. 58 A.D.2d 547 (1977). The complaint for damages was then dismissed by a justice of the Supreme Court; and again the Appellate Division affirmed, 63 A.D.2d 890 (1978). The Court of Appeals denied leave to appeal on October 31, 1978.

After Clarkson's appointment as trustee was affirmed by the Canadian Supreme Court, the Shaheen group sued again in New York state court to enjoin Clarkson from acting under a first mortgage on the refinery, alleging fraud in Clarkson's appointment. The court dismissed the complaint. Provincial Refining Company Limited and SNR Dover Incorporated v. Kleinwort Benson Ltd. and The Clarkson Company Limited (Sup. Ct., N.Y. Co. Index No. 03740/1976), aff'd, 67 A.D.2d 896 (1979). The Shaheen group then brought an almost identical suit to prevent Clarkson from acting on a second

mortgage on the refinery. This complaint was dismissed on November 7, 1977. Provincial Refining Company Limited and SNR Dover Incorporated v. Government of the Province of Newfoundland and The Clarkson Company Limited (Sup. Ct. N.Y. Co., Index No. 03960/1976), aff'd, 403 N.Y.S.2d 166 (1978).

Another suit sought to enjoin Ataka's assignee from enforcing any claims against NRC and PRC, alleging the assignments violated New York law. Again, the state court dismissed the complaint. Shaheen Natural Resources Company, Inc., Roy M. Furmark, Homer White, and SNR Holdings, Inc. v. Atlantic Trading (Delaware) Corp. (Sup. Ct. N.Y. Co., Index No. 07932/1976), aff'd 58 A.D.2d 532 (1977), motion to vacate denied, 59 A.D.2d 863 (1977).

The last of Shaheen's unsuccessful suits was one for damages against Sumitomo Bank, Ltd., Ataka's main bank in the refinery project, alleging that Sumitomo had

converted sums deposited with it by PRC. On January 21, 1977, this one was dismissed with prejudice. Shaheen Natural Resources Company, Inc., Roy M. Furmark, Homer White and SNR Holdings, Inc. v. The Sumitomo Bank Ltd. (Sup. Ct., N.Y. Co., Index No. 09810/1976).

4/ Even though NRC is a Canadian corporation, the district court applied New York law in determining the obligations of the directors to the creditors and trustees of the corporation. We agree that New York law applies. Fed. R.Civ.P. 44.1 requires parties to give written notice, in the pleadings or otherwise, of their intention to assert foreign law. Here, none of the parties claimed the applicability of Canadian law or asserted that it differs from that of New York. Each seems to have assumed that New York law governs. Hence, the district court was not obligated to take judicial notice of Canadian law and correctly

applied forum law. Corporacion Venezolana de Fomento v. Vintero Sales Corp., 452 F. Supp. 1108, 1112 n. 3 (S.D.N.Y. 1978), remanded. 607 F.2d 994 (2d Cir. 1979). Even if the issue were not waived. the presence of NRC's headquarters and several of its creditors in New York, and the fact that many of the transactions in issue took place in New York, are sufficient contacts to invoke the application of New York law intended to protect New York creditors. See Armstrong v. Rangaire Corp., 493 F. Supp. 390 (S.D.N.Y. 1980); Intercontinental Planning, Ltd. v. Daystrom, 24 N.Y.2d 372, 300 N.Y.S.2d 817, 248 N.E.2d 576 (1969).

5/ Defendants also claim that the trustee is barred from asserting a claim for waste of assets against them because the shareholders in whose behalf the trustee is suing would be estopped from raising that

claim. Alternatively, they claim that the sole shareholder of NRC, SRC, ratified the loans and hence the trustee may not sue on behalf of NRC. Because we find that the trustee may sue on behalf of the creditors for the breach of the fiduciary duty owed them by the directors, we need not examine the claim that the trustee may not sue on NRC's or the shareholder's behalf.

6/ It should be noted that we are not required to examine the assertions of Shaheen and of the Shaheen group that the jury's verdict was not supported by siffi-cient evidence. As these defendants never moved for a direct verdict, for judgment n.o.v., or for a new trial, these assertions of insufficient evidence need not be reviewed by us. Scientific Holding Co. v. Plessy, Inc., 510 F.2d 15, 28 (2d Cir. 1974). Nor is there any showing that we should

review the evidence as a matter of discretion in the interests of justice. As we have noted, there was ample evidence to support the jury's findings that NRC was insolvent in 1974 and 1975 and that Shaheen had breached the duty owned by directors to the creditors in causing NRC to make loans without fair consideration in those years. Likewise, there was ample evidence that the loans to the Shaheen group were due on demand and not in 1985 as the defendants claimed. Plaintiff offered expert testimony, outside auditor's reports, and internal accounting reports to prove that the loans were due on demand. We see no reason to disturb that finding.

7/ The three other initial lenders were Kleinwort Benson, First National Bank of Chicago, and the government of Newfoundland. When NRC went bankrupt, its various creditors filed claims in the following amounts: preferred creditors, $16 million, unsecured

creditors, $75 million; contingent creditors, $300 million. Its assets consisted primarily of the monies owed it by Shaheen and the Shaheen companies.

8/ After the jury returned its verdict, Shaheen and Rishell contacted the Credit Lyonnais Bank, and complained that the juror had been a "leader." who had tried to "hang" Shaheen, and that "as to a certain deal in the corporate area (between Shaheen and the Bank) that she blew the deal ...." The juror complained to the judge, who called in the lawyers for the defendants, told them of the harassment, and ordered them to tell their clients to cease all communications directly or indirectly with any jurors.

APPENDIX E

THE SECOND CIRCUIT DECISION DENYING PETITIONERS' PETITION FOR REHEARING BELOW

UNITED STATES COURT OF APPEALS
SECOND CIRCUIT

THE CLARKSON COMPANY LIMITED, as Trustee in Bankruptcy, appointed by the Supreme Court of the Province of Newfoundland, of the property of Newfoundland Refining Company Limited and Provincial Refining Company Limited,

Plaintiff-Appellee,

-v-

JOHN M. SHAHEEN, ROY M. FURMARK, ALBIN W. SMITH, PETER L. CARAS, PAUL W. RISHELL, SHAHEEN NATURAL RESOURCES COMPANY, INC., NEWFOUNDLAND REFINING COMPANY LTD., U.S.A. and FOUNDERS CORPORATION,

Defendants-Appellants,

PHILIP GANDERT, WILLIAM J. SHERIDAN,

Defendants.

Nos. 80-7664
80-7712
80-7754
80-7790

Filed November 20, 1981

Petitions for rehearing containing suggestions that the action be reheard in banc having been filed herein by counsel for the defendant-appellant, Roy M. Furmark, by counsel for the defendants-appellants, Peter Caras, Paul Rishell and Albin W. Smith, and by counsel for the defendants-appellants, John M. Shaheen, Shaheen Natural Resources Company, Ihc., Newfoundland Refining Company Ltd., U.S.A., and Founders Corporation,

Upon consideration by the panel that heard the appeal, it is

ORDERED that said petitions for rehearing are DENIED.

It is further noted that the suggestion for rehearing in banc have been transmitted to the judges of the court in regular active service* and to any other judge on the panel that heard the appeal and that no such judge has requested that a vote be taken thereon.

(signed)
A. Daniel Fusaro
Clerk

* Judge Cardamone was inducted after this court had concluded its consideration of the petition and of the suggestion. Judge Cardamone took no part in the consideration of this matter.

Opposition

DISTRIBUTED
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FILED
FEB 11 1982
ALEXANDER L. STEVAS,
CLERK

No. 81-1258

IN THE

Supreme Court of the United States

October Term, 1981

JOHN M. SHAHEEN, SHAHEEN NATURAL RESOURCES COMPANY INC., NEWFOUNDLAND REFINING COMPANY LTD., U.S.A. and FOUNDERS CORPORATION,

Petitioners,

against

THE CLARKSON COMPANY LIMITED, as Trustee in Bankruptcy, appointed by the Supreme Court of the Province of Newfoundland, of the property of Newfoundland Refining Company Limited and Provincial Refining Company Limited,

Respondent.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Second Circuit

RESPONDENT'S BRIEF IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI

JEFFREY BARIST
Attorney for Respondent
The Clarkson Company Limited
14 Wall Street
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EDNA R. SUSSMAN
KATHRYN L. BEDKE
WHITE & CASE
Of Counsel

February 11, 1982

QUESTIONS PRESENTED

1. Are Petitioners entitled to a review by this Court of the finding of the District Court, affirmed by the Circuit Court, that a trustee in bankruptcy of a Canadian corporation appointed by the Supreme Court of the Province of Newfoundland and affirmed by the intermediate Appellate Court in Canada and the Supreme Court of Canada, is entitled to maintain a lawsuit in the federal district court in New York pursuant to the doctrine of comity under the governing law of the State of New York?

2. Is Petitioner Shaheen entitled to a review by this Court of the findings of the jury, affirmed by the Circuit Court, that Petitioner Shaheen had violated his fiduciary duties to creditors under the governing law of the State of New York?

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New York Debtor and Creditor Law, §§270 *et seq.*	25
Section 273	3, 4, 5
Section 274	3, 4, 5
Section 276	4,5

No. 81-1258

IN THE

SUPREME COURT OF THE UNITED STATES

October Term, 1981

JOHN M. SHAHEEN, SHAHEEN NATURAL RESOURCES COMPANY INC., NEWFOUNDLAND REFINING COMPANY LTD., U.S.A. and FOUNDERS CORPORATION,

Petitioners,

against

THE CLARKSON COMPANY LIMITED, as Trustee in Bankruptcy, appointed by the Supreme Court of the Province of Newfoundland, of the property of Newfoundland Refining Company Limited and Provincial Refining Company Limited,

Respondent.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Second Circuit

RESPONDENT'S BRIEF IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI

OPINIONS BELOW

The opinion of the Court of Appeals affirming the decision below is reported at 660 F.2d 506 (2d Cir. 1981), and is duplicated in the Appendix to the petition at A80-A116. The special questions submitted to and answered by the jury in the District Court appear at A1-A5 of that Appendix. The District Court's findings and conclusions with respect to the cause of action reserved for decision to the court is duplicated in the Appendix to this brief at RA1.

STATEMENT OF THE CASE

The Nature of the Case

This action was brought by The Clarkson Company Limited ("Clarkson") as trustee in bankruptcy of two corporations, Newfoundland Refining Company Limited ("NRC") and Provincial Refining

Company Limited ("PRC"), corporations organized and existing under the laws of the Province of Newfoundland, Canada, engaged in the ownership and operation of an oil refinery in Newfoundland. NRC and PRC were part of a complex web of corporations which included defendants Shaheen Natural Resources Company, Inc. ("SNR"), Founders Corporation ("Founders"), and Newfoundland Refining Company Ltd. USA ("NRC-USA"), all of which were controlled by Petitioner John M. Shaheen.

Clarkson sued Shaheen, SNR, Founders and NRC-USA claiming that "loans" amounting to over $50 million made by NRC to those defendants were due on demand and seeking immediate repayment of the monies lent; that the loans were fraudulent conveyances made in violation of Sections 273 and 274 of the New York

Debtor and Creditor Law; and that a letter agreement and promissory note entered into in October of 1975 which purported to extend the due date of the "loans" was a fraudulent conveyance made in violation of Sections 273, 274 and 276 of the New York Debtor and Creditor Law. Clarkson also sued certain individuals, including Shaheen, who were directors of NRC when the "loans" were made and the promissory note was entered into, claiming that the directors had participated in or allowed the conveyances in breach of their fiduciary duties to NRC and to the creditors of NRC.

The claims made by Clarkson were presented to a jury during a two and one-half week trial. The jury, in response to special questions submitted to it, found that the "loans" made by NRC were due on demand (A1); that NRC

was insolvent when the "loans" and the promissory note were made (A4); that the "loans" were made in violation of Sections 273 and 274 of the New York Debtor and Creditor Law (A2); that the promissory note was made in violation of Sections 273 and 274 of the New York Debtor and Creditor Law and also in violation of Section 276 of the New York Debtor and Creditor Law (which requires a finding of intent to hinder, delay or defraud creditors) (A2-A3). With respect to the claims against the directors, the jury found that the directors had breached their fiduciary duties to NRC and its creditors both in connection with the making of the loans by NRC and in connection with the making of the promissory note in October of 1975. A3-A4.

The District Court, sitting in equity on the one claim for relief reserved to the court, found that the intention of the parties at the outset was that the loans be due on demand, that the October 1975 promissory note was made at a time that NRC was insolvent and was a fraudulent conveyance without consideration made with the intent to hinder, delay and defraud creditors. The District Court declared the note a nullity and set it aside. RA1.

The Appointment of Clarkson as Trustee in Bankruptcy

The adjudication of the bankruptcy of NRC and PRC by the Supreme Court of the Province of Newfoundland (the local trial court) on March 12, 1976, was made after a weeklong adversary hearing during which the Shaheen group vigorously contested the bankruptcy petition and

urged various arguments upon the Canadian Court, including that urged to this Court concerning an alleged conspiracy by Ataka to drive NRC and PRC into bankruptcy. At the conclusion of the hearing, the Newfoundland Court appointed Clarkson trustee in bankruptcy of both corporations. In April 1976, the creditors of NRC and PRC, meeting under the auspices of the official receiver (a Canadian government official) confirmed Clarkson as trustee. No complaint was made at that time or at any time thereafter to the Canadian court about Clarkson's appointment or about any of Clarkson's acts. The Bankruptcy adjudication was affirmed by the intermediate Appellate Court and the Supreme Court of Canada, the highest court in Canada.*

* The Court of Appeals' summarization of the record in the Canadian courts is found in the two decisions of the Circuit Court dealing with this case. See Clarkson v. Shaheen, 660 F.2d at 508-09; Clarkson v. Shaheen, 544 F.2d 624, 630-32 (2d Cir. 1976).

The application to the Newfoundland Bankruptcy Court resulted in the Shaheen group commencing litigation in New York, first to head off, and then to reverse the Newfoundland judgment by collateral attack on the bankruptcy adjudication, the Newfoundland court and the trustee. Six actions were started; each action asserted one or more of the allegations of conspiracy here urged as grounds for having this Court review the decision of the Court of Appeals. Each of these actions filed in State Court have been dismissed. These actions were summarized by the Court of Appeals in its opinion. 660 F.2d at 509, n.3.

The Conduct of Petitioner John M. Shaheen

Mr. Shaheen is the only director found liable below who has presented a petition for writ of certiorari to this Court. Mr. Shaheen controlled

NRC, personally received some of the "loans" from NRC and was a director and controlling person of each of the six corporations to which NRC "loaned" the money in issue. Mr. Shaheen directed the making of all of the "loans" and the resetting of the loans to be due in 1985 by means of the promissory note. 660 F.2d at 508, 510.

The jury's finding that NRC was hopelessly insolvent in 1974 and 1975 when the "loans" and the note were made was found by the Court of Appeals to be supported by "abundant evidence." 660 F.2d at 513. The Court of Appeals further found that there was "sufficient evidence to support the finding that the directors knew or should have known that the 'loans' were made when NRC was insolvent and without fair consideration." 660 F.2d at 513.

REASONS FOR DENYING THE WRIT

I.

NONE OF THE TRADITIONAL REASONS FOR THE GRANTING OF PETITIONS FOR A WRIT OF CERTIORARI ARE SET FORTH IN THE PETITION

The petition does not present any of the reasons on the basis of which certiorari is most commonly granted. The Petitioner presents no conflict between the circuits; no conflict on a Federal question between the Federal Court and the State Court of last resort; no conflict among State courts on a Federal question; and no important question of Federal law. See Rules of the Supreme Court of the United States, Rule 17. Rather, Petitioners' argument is based on a construction of State law. Petitioners contend without citation of authority that the courts below (a) "erred" in recognizing Clarkson under the principles of comity and dismissing for legal insufficiency Petitioners'

pleading charging that Clarkson should not be so recognized because its "appointment was tainted with fraud"; and (b) "erred" in the standard of liability applied with respect to the directors. Petitioners' Brief at 26. Based on these claims of error, Petitioners assert that this Court should "exercise" its "power of supervision." Petitioners' Brief at 27.

Since federal jurisdiction over this action was grounded in diversity, the courts below applied the law of the forum state (here, New York) on the substantive issues concerning comity and corporate law. Erie Railroad Co. v. Tompkins, 304 U.S. 64, 78 (1938); Meredith v. Winter Haven, 320 U.S. 228, 234 (1943). The doctrine of comity is recognized as part of New York's substantive law. See Hilton v. Guyot, 159 U.S. 113, 163-64 (1895); Greschler v.

Greschler, 51 N.Y.2d 368, 375-78, 434 N.Y.S.2d 194, 197-99, 414 N.E.2d 694, 698-99 (1980); Feinberg v. Feinberg, 40 N.Y.2d 124, 127-28, 386 N.Y.S.2d 77, 78-79, 351 N.E.2d 725, 727-28 (1976); Watts v. Swiss Bank Corp., 27 N.Y.2d 270, 279, 317 N.Y.S.2d 315, 322, 265 N.E.2d 739, 744-45 (1970); International Firearms Co. Ltd. v. Kingston Trust Co., 6 N.Y. 2d 406, 411, 189 N.Y.S.2d 911, 913-914, 160 N.E.2d 656, 657-58 (1959). Questions regarding corporate law, including those involving the powers, duties and liabilities of corporate directors, are solely within the province of state law. Burks v. Lasker, 441 U.S. 471, 478 (1979); Santa Fe Industries v. Green, 430 U.S. 462, 478-80 (1977); Cort v. Ash, 422 U.S. 66, 84-85 (1975); Smith v. Sperling, 354 U.S. 91, 95-96 (1957).

"[O]rdinarily" this Court will not accept and therefore will not review, "save in exceptional cases, the considered determination of questions of state law by the intermediate federal appellate courts." Huddleston v. Dwyer, 322 U.S. 232, 237 (1944). It is the "general policy" of this Court to "leave undisturbed" holdings by the Court of Appeals on a question of state law. Estate of Spiegel v. Commissioner of Internal Revenue, 335 U.S. 701, 708 (1949). This is particularly true, when as here, "the same finding is made by the District Court." Appalachian Power Co. v. American Institute of Certified Public Accountants, 80 S.Ct. 16, 18, 4 L.Ed. 2d 30, 32 (1959). Accord, Cort v. Ash, supra at 72-74, n.6; Commissioner v. Estate of Bosch, 387 U.S. 456, 462 (1967); Ragan v. Merchants Transfer & Warehouse Co., 337 U.S. 530, 534 (1949).

Indeed, where it later develops that the issue raised "primarily implicates" a question of state law and "presents no federal questions of substance" this Court has dismissed writs as improvidently granted. Wolf v. Weinstein, 372 U.S. 633, 636 (1963). There is no reason here for departing from the general rule of this Court. The courts below decided the issues of New York law in accordance with unbroken precedents set by the New York Court of Appeals.

THE RECOGNITION OF CLARKSON AS TRUSTEE IN BANKRUPTCY UNDER THE PRINCIPLES OF COMITY WAS CORRECTLY DECIDED BY THE COURT OF APPEALS IN ACCORDANCE WITH APPLICABLE STATE LAW

The District Court and the Court of Appeals twice reviewed and twice rejected the Petitioners' allegations that Clarkson should not be recognized under New York law relating to the recognition of foreign trustees in bankruptcy

because Clarkson's "appointment in Newfoundland was tainted with fraud." Petitioner's Br. at 29-30.*

The question of whether or not Clarkson should be recognized under the principles of comity was first addressed by the District Court and by the Court of Appeals in 1976 in connection with an application for a preliminary injunction brought by Clarkson to gain possession of the books and records of NRC and PRC maintained in New York. Petitioner Shaheen resisted that application on the grounds that the bankruptcy adjudi-

* While Petitioners repeatedly use the phrase "due process" throughout their petition, nowhere do they explain how the alleged conspiracy in Clarkson's appointment as trustee in bankruptcy could have been a defense to the causes of action for fraudulent conveyances and breach of fiduciary duties asserted. Those claims were decided by the jury on the basis of the elements of these claims--NRC's solvency, the fairness of the consideration given to NRC, the existence of an intent to defraud creditors and the conduct of the directors. None of these facts have anything to do with Clarkson's appointment.

cation and Clarkson's appointment as trustee was "fraudulent" and so against New York public policy that it should not be granted recognition by the New York courts. The District Court issued the preliminary injunction sought.

The Court of Appeals reviewed the preliminary injunction and affirmed the recognition of Clarkson under the principles of comity as expressed by the New York courts. The Court of Appeals correctly summarized New York law:

> "Under it [comity], New York courts recognize the statutory title of an alien trustee in bankruptcy, as long as the foreign court had jurisdiction over the bankrupt and the foreign proceeding has not resulted in injustice to New York citizens, prejudice to creditors' New York statutory remedies, or violation of the laws or public policy of the state. Cole v. Cunningham, 133 U.S. 107, 122-23, 10 S. Ct. 269, 33 L.Ed. 538 (1890). These exceptions are construed especially narrowly when the alien jurisdiction is, like Canada, a sister common law jurisdiction with procedures akin to our own. Canadian trustees in bankruptcy with appropriate authority

> have been held entitled to recognition, Waxman v. Kealoha, supra; cf. Oakes v. Lake, 290 U.S. 59, 61-63, 54 S. Ct. 13, 78 L.Ed. 168 (1933) (receiver with statutory or court authority should be recognized in foreign jurisdictions), and Canadian judgments have been held entitled to credit, International Firearms Co. v. Kingston Trust Co., supra. New York courts have given foreign trustees injunctive or related relief to obtain possession or property, see, e.g., Fincham v. Income from Certain Trust Funds of Cobham, 193 Misc. 363, 81 N.Y.S.2d 356 (1948); Union Guardian Trust Co. v. Broadway National Bank & Trust Co., 138 Misc. 16, 245 N.Y.S. 2 (1930), and Canadian courts have also given this form of relief to a trustee appointed in the United States, Williams v. Rice, [1926] 3 D.L.R. 225." Clarkson v. Shaheen, 544 F.2d 624, 629-30 (2d Cir. 1976).

The Court of Appeals reviewed the transcript of the Canadian bankruptcy hearing and the allegations of fraud in light of these principles, and found that there had been insufficient allegations of fraud made even to "cast doubt on the Canadian judgment." 544 F.2d at 630-1. Recognizing that the case might not be over, the Court of Appeals ob-

served that "appellants are free to introduce additional proof [of fraud] at a trial on the merits of this action", 544 F.2d at 631, but admonished that any such claim of fraud "must be pleaded 'with particularity'" under Rule 9(b). 544 F.2d at 630.

The affirmative defense which Petitioners sought to assert upon return to the District Court did not offer additional proof of fraud. The affirmative defense offered was a rehash of the same charges which already had been found insufficient by the Court of Appeals and by judges in five State Court actions filed by the Shaheen group interests. Consequently, the District Court held that the proposed affirmative defense sought to be asserted did not conform to the pleading requirements of Fed. R. Civ. P. 9(b), and, in any event, did not plead any facts which could give rise,

as a matter of law, to a refusal to grant comity to Clarkson. The Court of Appeals held that "[t]he district court's denial of the Shaheen defendants' motion to amend their answer to assert unparticularized allegations of fraud in the Newfoundland bankruptcy proceeding and Clarkson's appointment was proper." 660 F.2d at 614-615.* Indeed, the Court, in another context, summed up Petitioners' contention with the observation that "[t]he claims about fraud and conspiracy on the part of Ataka appear to have been nothing more than a smoke-screen without any merit." 660 F.2d at 514.

* In similar circumstances, the New York Court of Appeals affirmed for lack of particularity the dismissal of a claim of fraud in the procurement of a foreign judgment and held that the foreign judgment must be accorded recognition under the doctrine of comity. Greschler v. Greschler, 51 N.Y.2d 368, 434 N.Y.S.2d 194, 414 N.E.2d 694 (1980).

Contrary to Petitioners' assertion, the Court of Appeals did not adopt any "rule of law" (Petitioners' Br. at 27) in affirming the denial of leave to plead the affirmative defense. No precedent was set here which merits the attention of this Court. The Court of Appeals' and the District Court's decisions were based on an analysis of the particular pleading presented by Petitioners in light of the full record developed during the five-day hearing held in Canada, the subsequent affirmance of Clarkson's appointment by the Supreme Court of Canada, and settled standards for pleading fraud with particularity under Fed. R. Civ. P. 9(b). An application by a District Court of the Rules of Civil Procedure when affirmed by the Court of Appeals will not ordinarily be reviewed by this Court. This is so especially where, as here,

"the question is one that concerns the judgment of the District Court in relation to a particular set of facts." Appalachian Power Co. v. American Institute of Certified Public Accountants, supra, at 18. No basis for an exception to this general policy of this Court exists here.

THE LIABILITY OF MR. SHAHEEN WAS WAS CORRECTLY DECIDED BY THE COURT OF APPEALS IN ACCORDANCE WITH APPLICABLE STATE LAW

The Court of Appeals reviewed the applicable law of the State of New York as to the duty of directors to creditors and correctly affirmed the finding of the jury that these duties had been breached by Petitioner Shaheen on the facts presented at trial. Mr. Shaheen claims that the Court of Appeals erred because New York law does not permit the

finding of liability by a director to creditors where (a) the director received no funds (Petitioners' Br. at 58-59); and (b) the corporation was continuing in operation. Petitioners' Br. at 30, 61. These claims of error are made despite the fact that Mr. Shaheen, either directly or through transfers to his controlled corporations, received all of the funds from NRC and are made without benefit of supporting citations.

The general liability of directors to creditors first set forth by this Court in Wood v. Dummer, 3 Mason 308, Fed. Cas. No. 17,944 (1824), has been adopted in New York not only in the case law, but since 1829 has been the subject of statutory enactment. It is now included in Section 720 of the New York Business Corporation Law. Contrary to Petitioner's unsupported assertion, directors, including those who were not

the recipients of challenged transfers, have been repeatedly held liable by the New York court for damages resulting to creditors from their breach of duties. New York Credit Men's Adjustment Bureau v. Weiss, 305 N.Y. 1, 110 N.E.2d 397 (1953); Darcy v. Brooklyn & N.Y. Ferry Co., 196 N.Y. 99, 89 N.E. 461 (1909); Cullen v. Friedland, 152 A.D. 124, 136 N.Y.S. 659 (1st Dep't 1912); Sherwood v. Holbrook, 98 Misc. 668, 163 N.Y.S. 326, 332 (Sup. Ct. N.Y. Co.), aff'd, 178 A.D. 462, 165 N.Y.S. 514 (1st Dep't 1917). While it may be that in certain circumstances directors who have not received funds may not be liable to creditors, Petitioner Shaheen received, directly or indirectly, all of the funds in issue in this case.

The New York rule, that the directors' duty to creditors arises when the

corporation becomes insolvent is, as the Court of Appeals found, "plainly stated." 660 F.2d at 512. No other precondition to the creation of the trust relationship and to the directors' duties to creditors is imposed. The New York rule was set forth by the New York Court of Appeals in New York Credit Men's Adjustment Bureau, Inc. v. Weiss, supra:

> "If the corporation was insolvent at that time it is clear that defendants, as officers and directors thereof, were to be considered as though trustees of the property for the corporate creditor beneficiaries." 305 N.Y. at 7.

Accord, Sherwood v. Holbrook, supra, at A.D. 466; Ward v. City Trust Co. of New York, 192 N.Y. 61, 74, 84 N.E. 585, 589 (1908).

Petitioner Shaheen's sole citation in support of his contention that insolvency is not enough under New York law to trigger a director's fiduciary

duties to creditors (Petitioners' Br. at 61), is one general commentary on corporate law which does not even purport to be speaking of New York law and one court decision in which the court made no attempt to define the parameters of a director's duties to creditors, but referred to liquidation simply because the facts of the particular case happened to involve a liquidation. As the Court of Appeals found in this case, to hold, as Petitioner Shaheen urges, that no duty to creditors arises until it is clear that the corporation is no longer a going concern "flies in the face of the New York policy to preserve the assets of insolvent corporations for the creditors". 660 F.2d at 512.*

* Petitioner Shaheen mischaracterizes the issue by suggesting that his liability was found to exist under the New York Fraudulent Conveyances Act (New York Debtor and Creditor Law, §§270 et seq.). (Petitioners' Br. at 59-60,

[footnote continued]

Petitioner's doomsday prediction that corporate boardrooms across America "would empty" as a result of the decision below (Petitioners' Br. at iv-v) is foolish. Corporate boards across America do not give corporate assets to themselves without fair consideration -- an essential element in the holding against Mr. Shaheen in this case. Mr. Shaheen was found liable by the jury for engineering the giving away of corporate

[footnote continued]

63-64). Liability was found not under that Act but under the authorities here cited as to a director's duties to creditors. Petitioner further claims that allowing a trustee in bankruptcy to assert claims on behalf of unsecured creditors was "novel" (Petitioner's Br. at 59), ignoring Section 720 of the New York Business Corporation Law which lists a "trustee in bankruptcy" as a person who may bring an action thereunder as a representative of creditors against directors and officers and ignoring a long line of New York decisions to the contrary. See e.g., New York Creditmen's Adjustment Bureau Inc. v. Weiss, supra, 305 N.Y. at 8; Sherwood v. Holbrook, supra; Doyle v. Gordon, 158 N.Y.S.2d 248, 254 (Sup. Ct. N.Y. Co. 1954); Bartle v. Markson, 357 F.2d 517 (2d Cir. 1966).

assets to himself and to his controlled corporations, all at a time when the corporation was insolvent. The Court of Appeals, in affirming Mr. Shaheen's liability, did not regard its decision as making new law in New York. We would think that the proposition is generally unexceptionable.

CONCLUSION

For the foregoing reasons this petition for writ of certiorari should be denied.

Respectfully submitted,

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* All of the shares of Clarkson are owned by Clarkson Gordon, a partnership. Clarkson has no subsidiaries. Woods Gordon, a partnership, is the only affiliate of Clarkson.

APPENDIX

The Finding of the District Court Concerning the Promissory Note

"I do find, as the Court sitting in equity ... that the intention of the parties at the outset of these advances was that they be due upon demand, that as of October 1975 NRC was insolvent and that the note and related papers that were issued at the same time were a fraudulent conveyance without consideration with intent to hinder, delay and defraud creditors and as such I declare that it is a nullity and I have set it aside."